



MINERALS COUNCIL OF AUSTRALIA

SUBMISSION TO SENATE ECONOMICS REFERENCES
COMMITTEE
INQUIRY INTO CORPORATE TAX AVOIDANCE

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1. INTRODUCTION

About the MCA

The Minerals Council of Australia (MCA) represents Australia's exploration, mining and minerals processing industry, nationally and internationally, in its contribution to sustainable economic and social development. The MCA's strategic objective is to advocate public policy and operational practice for a world class industry that is safe, profitable, innovative, environmentally responsible and attuned to community needs and expectations. MCA member companies represent more than 85 per cent of Australia's annual minerals industry production and a higher share of minerals exports.

The MCA welcomes the opportunity to make this submission to the Senate Economics Committee and contribute to the corporate tax integrity debate.

Focus of the submission

The MCA supports the need for strong, balanced tax laws to protect the integrity of Australia's tax regime, and the MCA supports initiatives to increase tax transparency where they are meaningful and aid public debate.

The submission seeks to address the list of matters in the Inquiry terms of reference. In particular, this submission offers views on the adequacy of Australia's tax laws, ATO capabilities, tax transparency and opportunities to collaborate internationally to address tax avoidance and aggressive tax minimisation. Importantly, the submission addresses misrepresentations on the mining industry's tax contribution.

Importantly, this inquiry comes part way through the Organisation of Economic Cooperation and Development (OECD) Base Erosion and Profit Shifting (BEPS) project. A multilateral, co-ordinated international effort is the most appropriate way to modernise the international tax framework.

The inquiry also comes at the beginning of the Government's tax reform White Paper process. The MCA will play a constructive role in that process on tax integrity and broader corporate tax policy issues.

2. EXECUTIVE SUMMARY

The importance of fact based debate

Public confidence in Australia's tax system is vital to ensure voluntary tax compliance. There must be a level of trust that business, and individuals, meet their tax obligations and pay their 'fair share'.

It is important that the current debate on Australia's corporate tax system and the international tax framework is informed by facts rather than unsubstantiated rhetoric. False claims relating to taxpayers and industries have the potential to undermine public faith in Australia's tax system and unfairly harm corporate reputations. The ATO has underlined the importance of a fact based debate noting that:

Uninformed commentary about the tax performance of taxpayers and the performance of the ATO does nothing to improve the transparency or effectiveness of the tax system but actually works to undermine confidence in the system which impacts on willing participation.¹

Minerals taxation

- The tax take from the minerals industry (including Federal company tax and State royalties) has increased roughly four fold over the past decade. The mining industry accounts for 25 per cent of corporate tax receipts despite accounting for about 10 per cent of GDP.
- International comparisons of tax rates show that Australia is a relatively high tax mining jurisdiction.
- Official data confirms that Australian mining pays a relatively high effective corporate tax rate. Suggestions to the contrary rely on flawed approaches. Claims the mining industry receives large government subsidies are similarly baseless.

Australia's corporate tax regime

- Australia's corporate tax regime includes strict integrity rules and these have been strengthened in recent times. Australia also takes a disciplined approach to tax treaties.
- A number of Australian mineral resources companies are leaders when it comes to tax transparency. There is a need to ensure any government-mandated transparency measures are not used opportunistically in a way that misleads the public.

The way forward

- A multilateral, co-ordinated international effort is the most appropriate way to deal with aggressive tax minimisation strategies and modernise the international tax framework. Meaningful action to address base erosion and profit shifting should be coordinated through the OECD BEPS project in which Australia is taking an active role.
- Any proposed changes to Australia's already strong tax integrity rules should be carefully targeted at the 'tax mischief' identified.

¹ Andrew Mills, ATO Second Commissioner, Address to The Tax Institute's National Resource Tax Conference, 16 October 2014

3. TAXATION OF THE MINERALS INDUSTRY: THE FACTS

Mining's tax contribution

Mining is among the highest taxed industries in Australia. The mining industry pays significant amounts of tax in Australia and that contribution has increased in recent years.

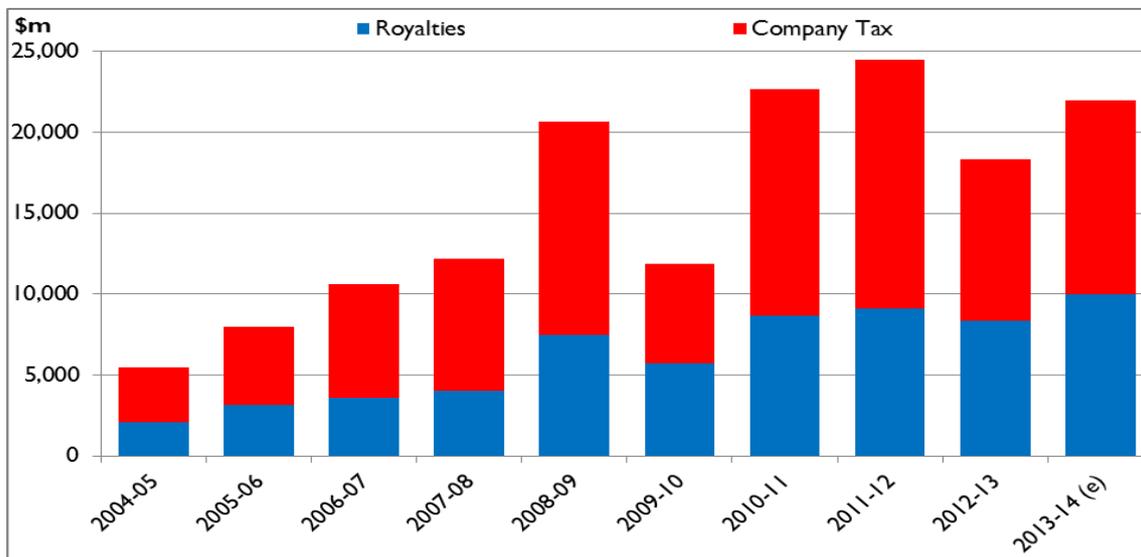
Company tax and royalties are the two main fiscal instruments used by Government to collect revenues from the mining industry. The mining industry makes a large tax contribution in Australia through these revenue sources. Official Australian Taxation Office (ATO) statistics and research by Deloitte Access Economics show that:

- In 2011-12, the mining industry paid over \$15 billion in company tax alone² - almost a quarter of all company tax in Australia while accounting for around 10 per cent of GDP.
- The total contribution from Federal company tax and State and Territory royalties from the minerals industry was \$156 billion between 2004-05 and 2013-14.³
- Over the last three years (2011-12 and 2013-14), the minerals industry's tax and royalty contribution is estimated to have been more than \$66 billion.⁴

Mining's tax contribution has grown markedly over the last decade.

- Company tax and royalty revenues (excluding oil and gas) have increased roughly four-fold over the past decade from \$5.5 billion 2004-05 to an estimated \$22 billion in 2013-14.
- Federal company tax on mineral resources companies has risen from \$3.4 billion in 2004-05 to an estimated \$12 billion in 2013-14.
- State mineral royalties have risen from around \$2 billion in 2004-05 to almost \$10 billion in 2013-14.⁵

Minerals industry company tax and royalties (2004-05 to 2013-14)



Source: Deloitte Access Economics, Estimated company tax, MRRT, carbon tax and royalties expenses for the minerals sector

² ATO, Taxation statistics 2011-12 <https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Tax-statistics/Taxation-statistics-2011-12/>

³ Deloitte Access Economics, Estimated company tax, MRRT, carbon tax and royalties expenses for the minerals sector, Report prepared for the Minerals Council of Australia, July 2014

⁴ Ibid.

⁵ Ibid.

The substantial increase in company tax payments over recent years has been driven by increased commodity prices and profitability. Despite recent falls in commodity prices, DAE estimates that the mining industry will pay \$12 billion in company tax in 2013-14 and \$10 billion in royalties.⁶

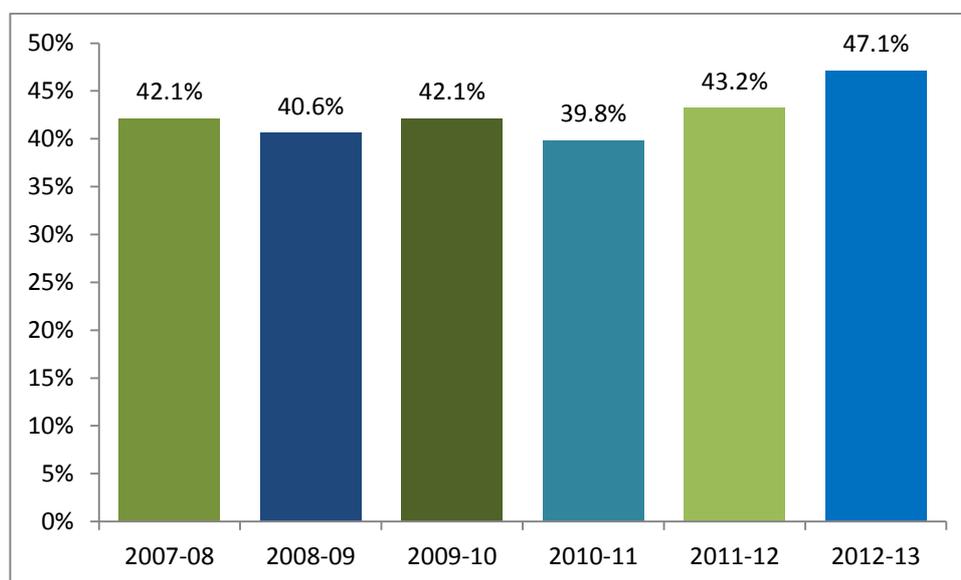
In addition to company tax and royalties, the minerals industry pays a large number of other taxes, charges and levies to Australian Federal, State and Local governments. These include payroll tax, Fringe Benefits Tax (FBT), land taxes, stamp duties and various local government charges.

Mining's tax take ratio is rising and is high by international standards

Mining pays a high effective corporate tax rate. When royalties are included, mining's effective tax has averaged in excess of 40 per cent over the last six years.

- The MCA-Deloitte Access Economics minerals industry tax survey finds that mining's effective marginal tax rate averaged 42.5 per cent between 2007-08 and 2012-13 when royalties are included.
- In 2012-13, the total tax take ratio rose for the third consecutive year reaching a new high of 47.1 per cent - in other words, nearly half of every dollar of profit made by the minerals sector is paid to the Federal Government in company tax and to State Governments in royalties.⁷

Mining's Total Tax Take



Source: Deloitte Access Economics, Minerals Industry Tax Survey 2014

The tax ratio increase in 2012-13 is attributable to falling commodity prices and mining profits without a corresponding fall in tax payments. This is because royalties are not linked to profits and royalty rates have been increased in some States in recent years. This trend in rising tax ratios is expected to continue.

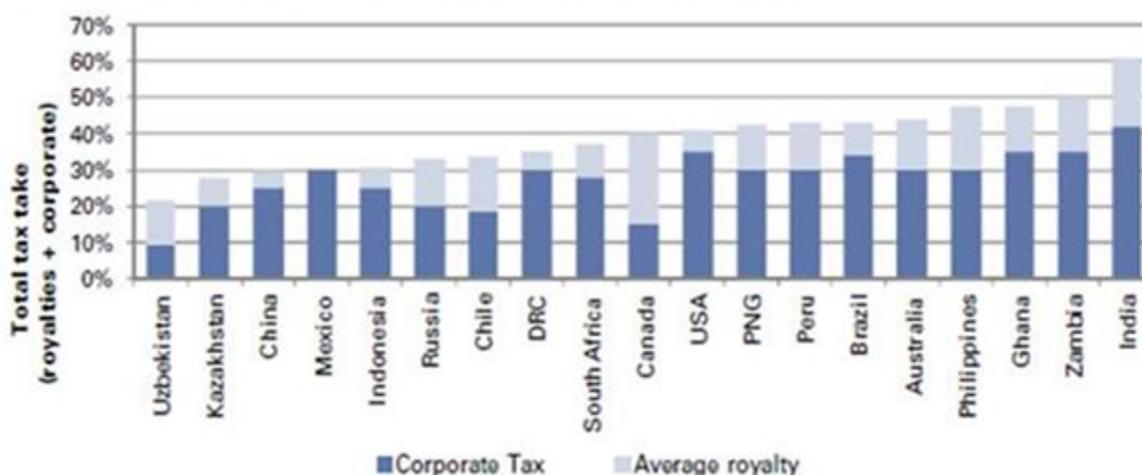
Australia's effective tax rate on mining is at the top end compared with other countries with large mining industries. A 2013 study by Goldman Sachs found that the tax take from Australian mining companies is within the top 25 per cent of global mining jurisdictions.⁸

⁶ Deloitte Access Economics, Estimated company tax, MRRT, carbon tax and royalties expenses for the minerals sector, Report prepared for the Minerals Council of Australia, July 2014

⁷ Deloitte Access Economics, Minerals Industry Tax Survey 2014

⁸ Goldman Sachs, Australia: Metals & Mining, "Resource nationalism poses big threat to miners", 23 January 2013.

Exhibit: Total tax take for major mining companies



Source: Company data, Goldman Sachs Research estimates.

Does mining pay a low effective tax rate compared to other industries?

Data from the ATO shows that mining's effective company tax rate was 27 per cent in 2011-12 compared to taxable income. This was well above the all industries average of 23 per cent.⁹

A recent Tax Justice Network (TJN) report 'Who Pays for our Common Wealth' claimed that Australian corporations 'appear to avoid tax obligations'. It also claimed that \$8 billion of revenues were forgone because the average effective tax rate across the corporate sector was less than 30 per cent. This was based on flawed calculations of accounting profits.¹⁰ Treasury labelled the forgone revenue argument as 'patently false' and 'fundamentally a misunderstanding of what taxable income in Australia ought to be about'.¹¹

Similarly, claims over recent years that mining pays an effective tax rate substantially below the headline company tax rate of 30 per cent are inaccurate. Estimates have ranged between 13.9 per cent according to the Australia Institute and 22 per cent according to the Australian Council of Trade Unions (ACTU).

Effective tax rates calculated by comparing tax paid to various measures of income including accounting income derived from financial statements and sector wide corporate profits (gross operating surplus and net operating surplus) derived from national accounts data provide misleading information. Comparing tax paid to accounting income, and not to taxable income, will always result in an effective rate which differs from 30 per cent. Income tax is levied on taxable income, not accounting profit (see Appendix A for further information).

Accounting income and taxable income are different concepts. Treasury and the ATO explained the difficulties of mixing accounting and tax concepts of income to calculate effective tax rates in the context of the TJN report's calculations. Neil Olsen of the ATO explained:

having a look at accounting profit as opposed to taxable income is meaningless to the extent that taxable income and accounting profits are two fundamentally different concepts.¹²

Rob Heferen of Treasury said:

⁹ ATO, Taxation statistics 2011-12 <https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Tax-statistics/Taxation-statistics-2011-12/>

¹⁰ TJN's calculations of accounting profit across the corporate sector contained serious errors. It included, for example, foreign income not subject to Australian tax and property trust income which is taxed in the hands of beneficiaries.

¹¹ Hansard, Estimates hearings, Economics Legislation Committee, 22 October 2014

¹² Hansard, Estimates hearings, Economics Legislation Committee, 22 October 2014

it is just comparing an apple with an orange and not being about fruit.¹³

Does the mining industry benefit from tax ‘subsidies’ or ‘loopholes’ to reduce its taxable income?

Low effective tax rates based on flawed comparisons between ‘corporate profits’ and tax paid are used to suggest the existence of ‘loopholes’ in the tax system. The TJN report, for example, refers to 2011 ACTU research on ‘tax concessions’ used by mining companies to ‘help minimise their tax payments’.

Claims that the mining industry receives large tax or government program ‘subsidies’ are baseless. They have been rejected repeatedly by the Productivity Commission, the Australian Treasury and respected analysts.

The Productivity Commission’s 2012-13 Trade and Assistance Review found that:

The estimated effective rate of assistance from tariff and budgetary assistance for mining is negligible.¹⁴

The bulk of what the Productivity Commission measures as assistance to mining takes the form of measures available to all industries, not just mining, such as specific Government policy incentives for R&D.

Treasury has stated that ‘Australia does not have any sector specific tax expenditures for fossil fuel production’¹⁵ noting that producers can access general measures that apply economy wide.

Professor Sinclair Davidson concluded from a detailed analysis of effective tax rates and Government industry assistance measures that:

the mining industry pays a substantial sum of money in corporate taxation and pays at a rate of close to 30% of its taxation income. ... The argument that mining pays a low percentage of its income in taxation is simply not true. The argument that mining pays a low proportion of total corporate tax is simply not true.¹⁶

¹³ Hansard, Estimates hearings, Economics Legislation Committee, 22 October 2014

¹⁴ Productivity Commission, Trade and Assistance Review 2012-13 <http://www.pc.gov.au/research/recurring/trade-assistance/2012-13>

¹⁵ AUSTRALIA’S SUBMISSION TO G20 ENERGY EXPERTS GROUP, document 10A <http://www.treasury.gov.au/~media/Treasury/Access%20to%20Information/Disclosure%20Log/2012/G20%20commitments%20on%20fossil%20fuel%20subsidies/Downloads/Document%2010A.ashx>

¹⁶ Sinclair Davidson, Mining Taxes and Subsidies: Official evidence, May 2012

4. AUSTRALIA'S CORPORATE TAX REGIME

Australia has strict tax integrity rules, a high corporate tax rate (30 per cent) and high reliance on company tax revenues by international standards. Treasury analysis has not identified systemic tax avoidance in Australia's corporate tax system, although there are emerging risks associated with globalisation and the growth of the digital economy. Treasury's Scoping paper on 'Risks to Australia's Corporate Tax Base' recently noted:

the view in submissions on the Issues Paper that there was relatively little evidence of widespread erosion of Australia's corporate tax base at present from tax minimisation activity by multinational enterprises. While data limitations make it difficult to be definitive, this reflects, amongst other things, actions by successive governments to ensure the integrity of Australia's tax laws, the relative effectiveness of the ATO in enforcing corporate tax law, and the good compliance behaviour of companies.¹⁷

Australia's tax integrity rules

Australia's strict tax integrity rules restrict the use of tax avoidance strategies. They include broad ranging Controlled Foreign Company (CFC), transfer pricing, thin capitalisation and general anti-avoidance rules (GAAR).

Australia's tax integrity rules have recently been further strengthened. Measures to increase the robustness of the transfer pricing, GAAR and thin capitalisation rules have been legislated over the last 18 months.

The ATO and Treasury have stated that Australia's corporate tax integrity rules are sufficient and strong. Rob Heferen, Executive Director of Revenue Group Treasury said that 'Australia has a comprehensive CFC regime, tough transfer pricing rules and extensive general anti-avoidance rules.'¹⁸

The ATO's Second Commissioner Andrew Mills stated late last year:

With changes over recent years, we have transfer pricing and anti-avoidance laws that are – if not the strongest - among the strongest in the world and we are not afraid to use them.¹⁹

The ATO actively scrutinises major transactions and enforces the law. Second Commissioner Andrew Mills added recently:

Any suggestion that we are going "soft" on large corporates avoiding their tax obligations could not be further from the truth. As I have previously said, it's important to have a debate but even more important to do so with "facts", not myths.²⁰

In addition to strong tax integrity laws, Australia has a comprehensive Tax Information Exchange Agreement (TIEA) network and takes a disciplined approach to tax treaties. TIEAs play an important role in addressing international tax avoidance and evasion practices by facilitating the sharing of information between tax authorities in different jurisdictions. A large number of TIEAs were entered into in recent years with Australia signing more than 30 agreements since 2010.

Australia's comprehensive TIEA network comes in addition to Australia's disciplined approach to tax treaties which reduces the risk of any possible tax treaty abuse.

Australia's adoption of the OECD's Common Reporting Standard in 2018 will further improve the ATO's ability to monitor any aggressive tax practices. It will provide for the automatic exchange of tax information on Australian companies' offshore activities with a number of overseas tax authorities.

¹⁷ The Treasury, Scoping Paper on Risks to Australia's Corporate Tax Base, July 2013

¹⁸ Rob Heferen, Address to the 2014 Economic and Social Outlook Conference, Melbourne Institute, 4 July 2014

¹⁹ Andrew Mills, Address to The Tax Institute's National Resource Tax Conference, 16 October 2014

²⁰ ATO Second Commissioner Andrew Mills, Address to the Australasian Tax Teachers' Association 27th annual conference, 20 January 2015

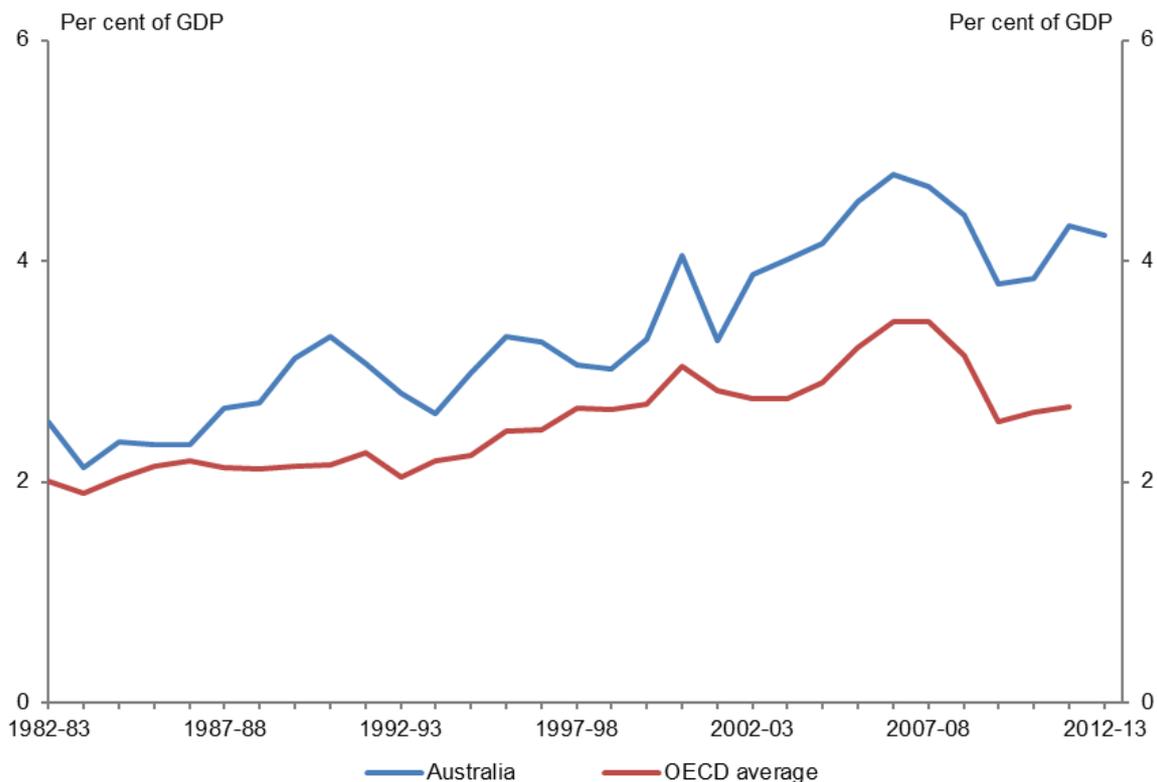
Australia's tax to GDP ratio

Although Australia has a lower overall tax to GDP ratio compared to the OECD average, Australia has a high corporate tax to GDP ratio compared to OECD countries and company tax accounts for a higher proportion of tax collected in Australia compared to OECD countries.

International comparisons on corporate tax show that:

- Australia's company tax as a share of GDP is second only to Norway in the OECD (with the two countries collecting large tax revenues from their resources sectors).
 - Company tax as a percentage of GDP in Australia is 5.2 per cent in 2012, compared to the OECD average of 2.9 per cent.²¹
- Company tax accounts for almost one fifth of Australian Government tax revenue - more than double the OECD average.
 - Company tax receipts accounted for 18.9 per cent of total federal taxation revenue in 2012 compared to the 8.6 per cent OECD average.²²
- Australia's company tax rate of 30 per cent is higher than the OECD average of 25.2 per cent and our competitors in the Asian region is 20.8 per cent.²³
- Australia ranks 24th out of 34 countries on corporate tax rate competitiveness.²⁴

Company tax receipts as a proportion of GDP



Sources: PBO based on data from the OECD, ABS and Treasury²⁵

²¹ OECD Statistics, Revenue Statistics - Comparative tables, <http://stats.oecd.org/index.aspx?DataSetCode=REV>

²² OECD Revenue Statistics, <http://stats.oecd.org/index.aspx?DataSetCode=REV>

²³ Tax Foundation, Corporate Income Tax Rates around the world, 2014.

²⁴ Tax Foundation, International Tax Competiveness Index

²⁵ PBO, Trends in Australian Government Receipts, 1982-83 to 2012-13, 01/2014

A major reason Australia has a high reliance on company tax is Australia's broad corporate tax base. The 1999 'Ralph Review' culminated in reforms which removed a number of tax depreciation allowances in a move towards a 'broader base, lower rate' corporate tax system.

The Parliamentary Budget Office (PBO) has noted that base broadening measures have 'improved the integrity of the tax system by removing opportunities for tax minimisation'. The PBO found that:

Measures to broaden the corporate tax base and improve compliance largely offset the impact of company tax rate reductions, so the proportion of company profits paid in income tax has not varied significantly over the last three decades.²⁶

Australia's increased reliance on company tax therefore came about despite cuts in the company tax rate.

Performance and capability of the ATO

It has been widely publicised that the Government has imposed broad ranging reductions in staffing at the ATO.

These staffing reductions have occurred at the same time as the ATO is implementing its 'reinvention' program following the appointment of Chris Jordan as the Commissioner of Taxation in January 2014. These changes have extended to bringing in experienced tax practitioners from accounting firms and law firms to the ATO's senior management group.

Key initiatives have been to foster willing participation, rethink compliance approaches and seek where possible the early resolution of tax disputes. This latter item has led the ATO to increase technical support for its audit teams and increase the use of alternate dispute resolution process (including through new ATO independent reviews) where appropriate.

MCA members have seen these cultural and procedural changes in practice, but the level of ATO review and audit activity has not diminished. In our view, recent criticism by some commentators of the ATO's ability to maintain revenue collections following the staff reductions is not warranted at this early stage.

²⁶ PBO, Trends in Australian Government Receipts, 1982-83 to 2012-13, 01/2014

5. THE WAY FORWARD: THE NEED FOR A MULTILATERAL APPROACH

As stated at the outset, the MCA agrees that companies must meet their tax obligations and any opportunities for alleged tax mischief should be addressed. A high level of tax system integrity is vital to ensure a fair tax system which can maintain the public's confidence. The most effective way to deliver this is by:

- Ensuring Australia has strong tax integrity rules;
- A multi-lateral approach with tax authorities working in a co-ordinated way to address tax avoidance; and
- Developing meaningful transparency measures.

Strong tax integrity rules

As noted above, Australia has strong tax integrity rules. However, vigilance is required to ensure any opportunities for tax mischief are dealt with.

Legislative changes should be measured and targeted. Integrity measures come with compliance costs and potential impacts on investment and legitimate activity. They should therefore be carefully considered, involve genuine consultation and only target the tax mischief. The former Government's proposed repeal of section 25-90 is an example of a poorly developed response to an integrity concern which would have impacted on Australian based companies expanding off-shore and imposed high compliance costs.

Further, ATO information sharing through TIEAs is an important part of the ATO's armoury to address any offshore tax evasion. The ability to share information is set to improve further with the automatic exchange of information initiative endorsed by the G20.

Multi-lateral approaches

Australia's tax rules do not stand in isolation. The current OECD BEPS project involves a comprehensive and multi-lateral approach to addressing opportunities for tax avoidance across a large number of jurisdictions. Acting in a co-ordinated way to address tax avoidance through the OECD BEPS project is the most effective means given the strength and recent updating of Australia's domestic tax integrity laws.

Treasury's Scoping Paper on Risks to the Sustainability of Australia's Corporate Tax Base concluded:

There are some actions Australia can and has taken unilaterally; these are primarily focused on improvements that can be made without significant divergence from international tax settings. But the key focus of Australia's efforts should be working multilaterally through international organisations to modernise international tax rules.²⁷

Tax Transparency

The minerals industry is supportive of efforts to improve the transparency of Australia's business tax system. Australian mineral resources companies have taken voluntary steps to increase tax transparency. The MCA is also engaging with government on opportunities to progress the outcomes of the Extractive Industries Transparency Initiative (EITI) pilot study supported by the MCA.

Australian mining companies are already among the global leaders on tax transparency. BHP Billiton and Rio Tinto have been recognised by Transparency International as two of the top three companies world-wide for transparency.

²⁷ The Treasury, Scoping Paper on Risks to Australia's Corporate Tax Base, July 2013

David Bradbury, Head of the Tax Policy and Statistics Division at the OECD and former Assistant Treasurer, noted in an address to the mining industry in 2013 that:

many listed companies, including some of the largest mining companies, should be commended for already disclosing a vast array of information about the tax they pay and their tax affairs.²⁸

He further acknowledged the industry's support for the EITI:

This is another area where Australia's mining industry is taking a world-leading role, and I again commend you for that.²⁹

The EITI and voluntary transparency initiatives by minerals companies open the mining industry to a greater level of tax transparency than is evident in any other industry in Australia.

Extractive Industries Transparency Initiative (EITI)

The Extractive Industries Transparency Initiative (EITI) promotes transparency in the extractive industries and host governments, with a primary focus on reducing corruption and enhancing development, particularly in resource rich developing countries. This is achieved through the regular publication of all material oil, gas and mining payments by companies to governments and all material revenues received by governments from oil, gas and mining companies (as assessed by a creditable independent auditor).

The global reputation of Australia's resources sector has been built on strong performance in the areas of ethical and sustainable mining practices. Accordingly, the MCA and member companies supported an Australian Pilot of the EITI to ensure that Australia is well placed to consider key issues relating to revenue transparency, including levels of risk, regulatory impact and administrative burden, when making a decision on whether or not to implement the EITI.

Domestically, the EITI pilot provided a multi stakeholder (government, industry and community) insight into Australia's disclosure and reporting of revenue in the Australian extractive resources sector, and the contribution that the sector makes more broadly to the national economy.

Increased transparency can improve public understanding of the tax system and tax payments, however to achieve this, transparency measures must provide useful, complete and accurate information to inform the public.

The former Government's tax transparency measure requiring the ATO to publish certain tax information of companies with annual income over \$100 million is an example of a tax transparency measure that provides simplistic and incomplete information to the public.

The 2013 legislation requires the ATO to publish company 'total income' (for which there is no concept in the tax law) including tax exempt income and unrealised accounting gains. This can be materially different to taxable income as it includes accounting amounts which can inflate 'total income' in a given year. The information published will not capture royalties paid by the minerals industry to State and Territory governments. Rather than improving public understanding, the release of taxpayer information in the form proposed (and without supplementary explanations) could lead to incorrect conclusions being drawn by the public on some companies' effective tax rates - precisely the opposite of the aim of increased transparency.

²⁸ David Bradbury, Address to the Minerals Council of Australia's Biennial Tax Conference, 16 April 2013

²⁹ Ibid.

APPENDIX A

Correct Application of the Income Tax Legislation will result in effective tax rates which differ from 30 per cent

Corporate income tax is levied on taxable income, not accounting profit. Taxable income and accounting profit are different concepts. Correct application of the income tax legislation will generally result in effective tax rates which differ from 30 per cent, where that effective tax rate is calculated by reference to accounting profit.

Taxable income will differ from accounting profit as a consequence of the following:

- Non-taxable income, such as foreign sourced income, being exempt for tax purposes but included in accounting profit. (Such foreign income will have been subject to taxes in the foreign country).
- Tax losses can be carried forward to offset future taxable income but are not fully reflected in accounting income.
- Timing differences for various types of expenses, including depreciation for capital expenditure, between the accounting standards and the taxation legislation.
- The R&D Tax Incentive provides a tax credit for R&D costs.
- Capital gains and losses are often calculated on a different basis for tax and accounting purposes.
- Fully franked dividends will be reflected in accounting profit but will not be subject to further taxation to the corporate shareholder.
- Accounting expenses such as impairment charges are not deductible for tax.