

By email: IntangiblesArrangements@ato.gov.au

16 June 2023

Timothy McCarthy
Angela Ho
The Australian Taxation Office

Dear Madam/Sir,

BDO SUBMISSION - DRAFT PRACTICAL COMPLIANCE GUIDELINE PCG 2023/D2 - INTANGIBLES ARRANGEMENTS

BDO refers to the invitation by Australian Taxation Office (ATO) to provide comments on the ATO's **Draft PCG 2023/D2 - Intangibles Arrangements**.

BDO is pleased to provide comments on the Draft PCG 2023/D2 (Draft PCG) which sets out the ATO's proposed compliance approach to Intangibles Arrangements involving international related parties. In summary, our main concerns regarding the Draft PCG are:

- The Draft PCG is not clear on the number of prior years the ATO expects a taxpayer to complete the risk assessment framework for intangible assets migrated or transferred in earlier years.
- The ATO should consider linking the proposed draft legislation (i.e. Treasury Laws Amendment (Measures for consultation) Bill 2023: Deductions for payments relating to intangible assets connected with low corporate tax jurisdictions and this Draft PCG, so arrangements that are assessed as low-risk can be considered as a ground for allowing deductions of payment related to intangible assets in low tax jurisdictions.
- The requirement to maintain the expected documentation and evidence at the time of seeking entry to an advance pricing arrangement (APA) program should be reconsidered as it could demotivate taxpayers looking for certainty on their intangible arrangements.
- There should be consideration of a materiality threshold as there is currently no materiality threshold for the application of the Draft PCG.
- The ATO should consider introducing a 'best effort' criterion as part of this Draft PCG to assist in providing more clarity to taxpayers in mitigating potential penalties.
- The ATO should consider introducing an additional risk mitigating factor (i.e., deduct points) where a taxpayer is able to substantiate the price of the intangible asset was 'stepped up' and

transferred at a higher value to an overseas related party.

- There is a lack of certainty as to when the documentation and evidence collated by the taxpayer would be sufficient, in cases where the ATO might use the benefit of hindsight e.g. when incorrect assumptions were used in commercial valuation, etc.

BDO's detailed comments in this regard are in the attached appendix.

Should you have any questions or wish to discuss any of the comments made in our submission, please do not hesitate to contact me on 02 9240 9736 or lance.cunningham@bdo.com.au.

Yours sincerely

Lance Cunningham

BDO National Tax Technical Leader

BDO Submission to the Australian Taxation Office Draft Practical Compliance Guideline PCG 2023/D2 - Intangible Arrangements

BDO has considered the Draft Practical Compliance Guideline PCG 2023/D2 (Draft PCG 2023/D2) - Intangible Arrangements relating to intangibles assets for public consultation and comments. This Draft PCG 2023/D2 provides the ATO's proposed compliance approach and risk assessment framework relating to arrangements involving intangible assets and international related parties. We provide the following comments on the issues of concern in the Draft PCG 2023/D2.

Clarify timing for back filling the documentation and risk assessment

The Risk Assessment Framework under Table 2 at Paragraph 45 notes as follows:

“If your Intangible Arrangement relates to, or is intrinsically linked to, intangible assets or products in connection with intangible assets that have previously been held (legally or beneficially) by you, also complete Risk Assessment Framework Table 1 of this Guideline in relation to the Migration if it involved an international-related party.”

In applying Risk Assessment Framework Table 1 of this Guideline to assess the compliance risks in relation to the Migration, answer each question based on the circumstances as at the time of the Migration.”

BDO suggests that the ATO provide further clarity with respect to the statute of limitations outlined in s815-150 of ITAA97 (i.e. regarding Amendment of assessments) against the expectations established in the draft PCG to evaluate and assess the risk in relation to migration of intangible assets as at the time of the migration. Specifically whether the disclosures should be limited to transfers of intangibles in the current year and prior two years as a practical matter.

On a related point, BDO also suggest that the ATO considers exempting taxpayers from assessing the risk rating of their intangible assets migrated previously if the transaction was subject to a review in the prior period - e.g., under an advance pricing arrangement (APA), a settlement agreement, a court decision, or a review under the justified trust /other similar programs. This would assist in reducing the compliance burden expected by the ATO under this draft PCG.

Interplay between this PCG and the proposed denied deduction legislation

As established in paragraph 4 of the drafted PCG, the ATO's “compliance approach with respect to the proposed multinational tax integrity measure - “denying deductions for payments relating to intangible assets connected with low corporate tax jurisdiction” is not covered by this Guideline.”

We note that there is an anomaly as on one side, the ATO expects taxpayers to assess the risk under this draft PCG and on the other hand, the draft legislation (i.e. Treasury Laws Amendment (Measures for consultation) Bill 2023: Deductions for payments relating to intangible assets connected with low

corporate tax jurisdictions) require the taxpayer to not claim any tax deductions under proposed s26-110 of ITAA 1997 where the payments are made to a related party in a low tax jurisdiction.

BDO recommends that if and when the proposed draft legislation is passed into law, the ATO considers linking the proposed draft legislation and this PCG, so arrangements that are assessed as low-risk (i.e. evidencing that the overseas related party satisfies the substance-based test provided under this draft PCG) can be considered as a ground for allowing deductions of payment related to intangible assets in low tax jurisdictions.

Simplifying Taxpayer's approach to an APA program

Taxpayers often approach the ATO to obtain certainty with respect to their complex situations/transactions and work towards reaching an agreement by utilising the Advance Pricing Arrangement (APA program). However, the current version of the **draft PCG in paragraph 21** suggests that the taxpayers should conduct a risk assessment and maintain detailed documentation when seeking entry to the APA program and during the APA program. We are of the view that this requirement will potentially discourage taxpayers who seek tax certainty from participating in the program.

Additionally, BDO believes the requirement could become counterintuitive and the taxpayers with lower risks or taxpayers maintaining the set of documentation as recommended by this PCG may choose to not approach the ATO altogether. This could lead to situations wherein the ATO will need to apply more compliance resources to assess these transactions at a later point in time.

Materiality threshold

We note that the **draft PCG at para 49** refers to the ATO considering the taxpayer's:

".....business systems and governance processes, including any appropriate materiality thresholds that you apply or follow in the business in relation to the management or governance of your or your global group's, intangible assets, to focus on evidence that can reasonably be expected to be created and relied on in your business."

While we appreciated this, BDO recommends that the ATO provides a materiality threshold or high-level assessment tool as to satisfy the overall risk in line with potential 'risk to revenue' ratio. This should assist in reducing the burden of compliance requirements for entities that are undertaking transactions that are not significantly material.

Evidence expectation vs best efforts

Due to the complexity involved in pricing intangible arrangements, BDO recommends that a 'best effort' criterion is introduced as part of this draft PCG. This should assist in providing more clarity to taxpayers in mitigating potential penalties if the ATO takes a different position in the pricing or form of such arrangements if a significant level of documentation and evidence exist (i.e., best effort).

BDO recommends that the ATO provides clarity on the evidence or a guide required to obtain greater certainty that the taxpayer has proceeded with their best effort and that they have done all that they can to ensure the transfer of intangible assets is conducted appropriately from an Australian perspective and that by taking these steps, the taxpayer will be provided assurance that the risk is reduced.

Additional risk mitigating factors

We understand that “**Risk Assessment Framework Table 1: Risk factors for Migration of intangible assets**” enables taxpayers to deduct points where the “relevant entity is resident in the jurisdiction which is also the jurisdiction in which the products or services related to the Relevant Intangible Assets are predominantly sold”.

On similar lines, BDO also recommends that the ATO introduce an additional risk mitigating factor (i.e., deduct points) specifically for situations where the taxpayer is able to substantiate that the price of the intangible asset was ‘stepped up’ and transferred at a higher value to an overseas related party. By increasing the revenue base in Australia, the PCG should therefore consider the outcome of such an arrangement to be lower risk.

Reasonable commercial evidence

BDO notes that the **draft PCG at Table 1 - Part C - Tax outcomes of the Intangibles Arrangement (point 6)** states as follows:

“Add **10 points** if:

- as a result of the restructure or change to your intangible assets, excluding capital gains^[16] from the disposal of the intangible assets, your taxable income is, or might reasonably be expected to be, less than it would have been if the restructure of, or change associated with, the Relevant Intangible Assets had not been entered into”

It is important to recognise that the decision to transfer the Intangible Assets are based on the information available to the parties at the time of entering into the transaction and that these considerations are not viewed in a different light as a result of hindsight. Therefore, we question the merits of the above points being applied as a result of hindsight.

BDO recommends that the ATO provides certainty as to when the documentation and evidence collated by the taxpayer would be sufficient, i.e. that the ATO would not use the benefit of hindsight for example when incorrect assumptions were used in commercial valuation, etc.