IT 2311 - Income tax : remission of additional tax imposed by section 225 where Division 13 of the Income Tax Assessment Act or comparable double tax treaty provisions are applied

TAXATION RULING NO. IT 2311

INCOME TAX : REMISSION OF ADDITIONAL TAX IMPOSED BY SECTION 225 WHERE DIVISION 13 OF THE INCOME TAX ASSESSMENT ACT OR COMPARABLE DOUBLE TAX TREATY PROVISIONS ARE APPLIED.

F.O.I. EMBARGO: May be released

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REFERENCE NO:	SUBJECT REFS:	LEGISLAT. REFS:
I 1209429	REMISSION OF ADDITIONAL (PENALTY) TAX	225 227(3)

PREAMBLE By way of background it should be noted that no additional tax was imposed under the repealed Division 13 (better known as section 136) or related double tax treaty provisions. However, from 28 May 1981 when the revised anti-profit shifting provisions of the law were invoked, additional tax at the rate of 10% per annum applied, pursuant to sub-sections 226(2B) to (2F), to relevant transactions entered into on or after that date. While the Commissioner has power to remit this additional tax, the law was seen as expressing a general legislative intention that the taxpayer should be left to bear the full statutory penalty. This additional tax was superseded by that provided for in section 225 which applies to relevant transactions entered into on or after 14 December 1984.

2. This ruling provides guidelines for the exercise of the Commissioner's discretion under sub-section 227(3) to remit the additional tax imposed by section 225.

3. Remissions of additional tax are to be considered under the two categories in respect of which section 225 imposes additional tax :

(i) profit shifting arrangements entered into for the sole or dominant purpose of avoiding liability to Australian tax; and

(ii) other profit shifting arrangements where tax avoidance is not the key purpose of the arrangements.

RULING Arrangements where tax avoidance is not the dominant purpose

4. The majority of profit shifting arrangements are unlikely to be blatant schemes entered into for the sole or dominant purpose of avoiding tax. Where tax avoidance is not the key purpose of the arrangements paragraph 225(1)(e) imposes

additional tax at the rate of 25% per annum of the extra tax payable as a result of the application of Division 13 or a related treaty provision, measured from the due date for lodgment of the taxpayer's return to the date when an original or amended assessment under these provisions is raised. The rate was previously 10% per annum.

5. While the Commissioner has power to remit the statutory additional tax, the question of remission needs to be considered against the general legislative intention in introducing the penalty provisions. From a revenue point of view, the legislature clearly regards profit shifting arrangements as unacceptable as other forms of tax avoidance or evasion. The penalty provisions represent, therefore, a signal that firms ought to be steering clear of profit shifting practices or, at least, from reliance on them in the presentation of their annual tax returns. In other words, tax conduct in this area should attain a standard where the anti-profit shifting provisions do not need to be invoked.

6. In addition to discouraging the use of profit-shifting practices, the rate of additional tax is an indication to firms engaging in profit shifting practices that they will not be allowed to benefit financially from avoiding their proper liabilities to Australian tax.

7. Against this background, it is clear that the legislature did not intend the remission power to be generally exercised to reduce the statutory additional tax.

8. At the same time, the imposition of a more severe penalty of 200% of the tax avoided, imposed under paragraph 225(1)(d) for cases of blatant schemes designed to avoid tax, makes it inappropriate that additional tax at the rate of 25% per annum should exceed, in any year, 200% of the extra tax payable as a result of the application of Division 13 or a related treaty provision. Remission would be warranted in these circumstances to ensure that the 200% upper limit was not exceeded.

9. Remission may also be warranted in circumstances where a taxpayer makes a prepayment of tax in relation to the anticipated application of Division 13 or a related treaty provision before an original or amended assessment is made pursuant to the anti-profit shifting provisions. In such cases the rate of 25% per annum should be applied to the period measured from the due date for lodgment of the return until the date on which the payment was made.

10. Remissions in other cases are expected to occur only in very limited and exceptional instances. In such cases the facts and a recommendation should be referred to Head Office for consideration.

Arrangements where tax avoidance is the sole or dominant purpose

11. Paragraph 225(1)(d) equates some international profit shifting arrangements with tax avoidance and evasion practices. Additional tax of 200% of the tax avoided is payable where the arrangements are blatant schemes entered into with the sole or dominant purpose of avoiding Australian tax - "scheme" has the same meaning as it has in Part IVA of the Act.

12. The new provisions impose additional tax on the same basis as sections 224 and 226 which concern other tax avoidance schemes and Part IVA schemes, respectively. The guidelines issued for the remission of additional tax levied under those provisions - Taxation Ruling No. IT 2312 - are also relevant in determining remissions of tax imposed by paragraph 225(1)(d). However, in considering the extent to which the additional tax under 225(1)(d) should be remitted, regard should also be had to the statutory penalty of 25% per annum that the taxpayer would have incurred if additional tax had been imposed under paragraph 225(1)(e). It would be anomalous if the taxpayer were to end up with a more favourable result under paragraph 225(1)(d). Therefore, the statutory penalty under that paragraph, after remission should not be less than the penalty that would be imposed by paragraph 225(1)(e).

13. The basic penalty of 40% flat of the tax avoided (the culpability component) plus 20% per annum, assumes co-operation with official enquiries. In international profit shifting cases, the amount of any additional tax to be imposed for lack of co-operation will depend on the readiness with which relevant information is provided and the completeness of that information.

14. Depending on the degree of seriousness of the offence the culpability component should be increased by 10%-50% of the tax avoided for circumstances where, for example -

(i) deliberate steps have been taken, either before or after commencement of official enquiries, to conceal the avoidance of tax;

(ii) there has been a lack of co-operation such as to cause undue/excessive delay in the completion of official enquiries and/or there has been obstruction or hindrance. The entity under review is expected not only to assist by the provision of all relevant information in its possession but also to do all in its power to facilitate the obtaining of information from its associated entities;

(iii) there has been previous participation in profit-shifting, tax avoidance or evasion practices by or on behalf of the taxpayer.

15. As the per annum component of the basic penalty is intended to reflect the length of time a taxpayer has had the use of moneys properly payable to the revenue, the fact that a taxpayer has made a prepayment of tax in anticipation of the application of the anti-profit shifting provisions should be taken into account in the calculation of the per annum

component. The same principles apply in these circumstances as apply in the remission of additional tax imposed by paragraph 225(1)(e) referred to in paragraph 9 above.

16. Also, as in the case of additional tax imposed by paragraph 225(1)(e), remissions in other cases are expected to occur only in very limited and exceptional instances. Again, such cases should be referred to Head Office with a recommendation.

COMMISSIONER OF TAXATION
18 June 1986