IT 2514 - Income tax: company Schedule 25A : information return for companies that transact business with related overseas entities

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TAXATION RULING NO. IT 2514

INCOME TAX: COMPANY SCHEDULE 25A : INFORMATION RETURN FOR COMPANIES THAT TRANSACT BUSINESS WITH RELATED OVERSEAS ENTITIES

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PREAMBLE The purpose of this Ruling is to identify the situations where a company is required to complete a Schedule 25A for inclusion with a Company Return Form.

BACKGROUND

2. The Overseas Transactions Information Schedule - 25A was introduced for companies on the 1986 return. Its introduction was a response to the ATO's increasing awareness of the taxation implications of international transactions. Whilst the information required by the schedule is not used in the assessment process, it is used to monitor the incidence and dollar value of transactions with related overseas entities. This can assist in determining audit priorities. The provision of accurate detail may obviate the need for audits or may assist in deciding whether an audit can be limited to particular matters only. The information on the Schedule is to be provided pursuant to Regulation 9 of the Income Tax Regulations. This Regulation governs the provision of other documents and information with return forms. Failure to provide a completed Schedule where appropriate, may attract penalties or prosecution under the law.

RULING 3. Potentially, the schedule applies to all companies that lodge income tax returns in Australia. This includes both resident companies and non-resident companies trading in Australia through permanent establishments or branches. A company is required to lodge a schedule if it satisfies two basic conditions. These conditions are firstly, that the company is related to an overseas entity. Secondly, where the company is related to an overseas entity, it engaged in any transaction with that entity during the tax year in question.

RELATED

4. For completion of Schedule 25A to be required, it is necessary for a relationship to exist between entities. The basic tie in this relationship is a participation by either entity in the management, control or capital of the other. The participation can include a right of participation, the exercise of which is contingent on an agreed event occurring. This "contingency" situation exists in so-called blind-trusts where secret agreements and other artificial devices are used in attempts to create the impression that there is no relevant relationship. In the case of a blind-trust these devices attempt to conceal the fact that a certain person, usually an Australian resident, is the beneficiary of the trust which is usually settled in a tax haven.

5. A related overseas entity in relation to an Australian company is defined in the Schedule 25A to include:

- any overseas entity which participates directly or indirectly in the management, control or capital of the Australian company;

- any overseas entity in respect of which the Australian company, directly or indirectly, participates in the management, control or capital;

- any overseas entity 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 the management, control or capital of the Australian company;

- any non-resident individual who participates directly or indirectly in the management, control or capital of the Australian company.

6. Entities can also be related through the intervening agency of a financial adviser. For example, an adviser may guarantee or arrange for a third party to guarantee, an international transaction.

7. The overseas entity can be of any type including, but not necessarily limited to, companies, their permanent establishments, trusts, partnerships and individuals. A key point is that the word "entity" as used in Schedule 25A includes branch offices and trusts.

8. The concept of participation mentioned above includes both direct and indirect participation. Direct participation covers the obvious situations such as shareholdings of 15% or more, trusteeships, directorships and partnership shares.

9. Indirect participation covers many varied situations. Discretionary trusts and nominee companies are two of the more obvious ones. Also included is the situation where an entity controls both an Australian company and an overseas entity. This indirect participation is capable of extending through a series of relationships. To use an extreme example, Mr X (an Australian

resident) is a director of a Hong Kong company (A) which in turn is a shareholder in a U.S. company (B). Mr X also is the sole shareholder in an Australian company (C) which is the trustee for a discretionary trust (D). C, as a trustee, is a partner in a U.S. joint venture (E). Mr X, A, B, C, D and E would all be considered as related entities. The determining factor to be considered is that if a participatory connection in the nature of management, capital or control exists, and various entities are linked in this way, the entities are related.

TRANSACTION

10. The other condition is that the company must engage in transactions with a related overseas entity in the year of income in question.

11. Transactions are divided into four categories on the schedule; tangible property, intangible property, services and other transactions. A transaction is considered to have been engaged in if any of the items listed have been supplied or acquired by the company lodging the schedule. For example, if an Australian branch of an overseas company has management services provided for it by its overseas head office, this constitutes a transaction for the purposes of the schedule.

12. As the schedule states, transactions may be by way of sale, exchange, lease, hire or hire purchase, providing, granting or conferring. These words do not pretend to provide an exhaustive definition of 'transaction'. As to what exactly constitutes a transaction, considerable judicial authority exists to give the word a very broad interpretation, viz.;

- "It is a comprehensive word which includes any dealings with property" (Barron (Inspector of Taxes) v Littman [1953] AC 96 at p.113).

- "Can embrace a number of activities" (Samuels v Peter F Burns Pty Ltd & Ors [14 SASR 1976] 88 at p.95).

- "Can cover a series of steps linked together to attain a definite objective" (Palmer v Comm'r of State Taxation [1976] WAR 37 at p.41).

- "Can cover a series of acts or steps linked together to attain a definite objective, and the understanding between the parties need not be of a legally binding character". (Robertson v Comm'r of Inland Revenue [1959] NZLR 492 at p.496).

13. The cases referred to above dealt with the concept of transaction in various contexts. They show the scope of the work and can provide guidance in determining what exactly constitutes a transaction.

14. For the purposes of the schedule, a transaction has been engaged in when it has been completed. The requirement to report the transaction does not have effect then until the transaction

has been completed. This is, from the lodging company's perspective, when the supply or acquisition has taken place. For example, if the lodging entity contracts to provide a service in one financial year but actually provides it in the following year, then the duty to report does not apply until the year in which it was provided. If, however, a transaction consists of a series of steps (e.g. instalments) each instalment will represent a separate transaction for reporting purposes.

15. The schedule separates transactions into four broad categories. These categories are: tangible property, intangible property, services and "other" transactions. The categories make distinctions that are not necessarily economic or legal distinctions; they are merely distinctions made for the particular purpose of the schedule. The final note to be made about transactions is that there need not be any consideration passing between the parties for a transaction to qualify for the schedule. It is important merely that a supply or acquisition has occurred.

TANGIBLE PROPERTY

16. This category includes real and personal property. All property involved in the process of manufacture is included i.e., raw materials, plant and equipment, trading stock and the finished product. Other tangible property may include personal property such as company shares and leasehold interests in land.

INTANGIBLE PROPERTY

17. This category covers a wide range of property including industrial and intellectual property. These include literary, artistic and scientific works, artistic performances and broadcasts, inventions, scientific discoveries, industrial designs, trademarks, commercial names and business goodwill. An example of a transaction of this type would be a company in Australia acquiring the Australian rights to use a certain brand name from its overseas parent.

SERVICES

18. This category covers any activity of a service oriented nature. Apart from those listed, this may include such diverse services as agency type services, warehousing, printing and editorial services, public relations, tolling services, feasibility studies, surveys, training etc.

OTHER TRANSACTIONS

19. This category includes items which are not easily categorised, such as loans, royalties and commissions. Other transactions falling into this category may include reimbursements.

COMMISSIONER OF TAXATION
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