BRITISH AMERICAN TOBACCO
AUSTRALIA

APPENDIX A

SUBMISSION BY BRITISH AMERICAN TOBACCO AUSTRALIA LIMITED ON THE REVIEW OF INTERNATIONAL TAXATION ARRANGEMENTS

BACKGROUND TO BRITISH AMERICAN TOBACCO AUSTRALIA LIMITED (BATA)

- BATA is an Australian resident company which is ultimately owned 100% by BAT plc in the UK.
- BAT plc is a company listed on the UK stock exchange.
- BATA holds shares in companies carrying on active businesses throughout the Pacific region including operations in Fiji, Papua New Guinea, New Zealand, Solomon Islands and Western Samoa.

INTERNATIONAL TAX REFORM IN CONTEXT

- As a nation, Australia has many positive attributes for attracting business investment including a strong growing economy, a skilled workforce and a stable political environment.
- Taxation and the complexity of the tax regime will always remain an important consideration in business investment decisions.
- There is increased evidence of countries throughout the world negotiating arrangements and implementing policies which seek to encourage the free flow of investment.
- Examples of the above include the following:
  - a European Union Directive under which withholding tax is removed for dividend flows between a parent company resident in one EU member State and a subsidiary company resident in another EU member State,
  - the UK currently has no domestic legislation that it imposes withholding tax on dividends,
  - renegotiation of the UK treaty with the US under which withholding taxes on royalties and interest are generally reduced to zero and a revised capital gains tax article which provides that gains on assets (including the sale of shares) in non real estate companies are exempted from United States tax,

- the UK Government's introduction of a capital gains tax exemption system for shareholdings of over 20% which have been held consistently for over twelve months,
- reform in Europe has seen the removal of domestic law imposing capital gains tax in Germany with effect from 1 January 2002, and
- the introduction of investment incentives in a number of countries throughout the Asian region, in particular Singapore.

- When seen in the light of the above, it is imperative for Australia to maintain a positive economic position by ensuring that its tax system does not discourage potential investment when compared to other jurisdictions.
- In light of the above it is essential that changes to the tax system be considered and evaluated not merely by reference to revenue implications but rather with a view to protecting and improving the long term viability of Australia as a vibrant and growing economy.

CONDUIT RULES

- It would appear apparent that recent changes to Australia's tax rules have not been sufficient to realistically establish Australia as a destination for setting up regional holding companies.
- Much of the reasoning for this lies in the fact that there is likely to be a significant income tax costs on the sale of shares in subsidiaries owned by the Australian company where the overseas business has been successful.
- There appears to be limited logic in Australia seeking to tax the gains arising from the disposal of shares held in foreign subsidiaries when, in contrast, income derived by such companies can be paid to the Australian parent as dividends and can flow through Australia to the ultimate non resident parent company without giving rise to any Australian tax in circumstances where an active business is being carried on by the foreign subsidiary.
- Whilst a complete "conduit regime" would be beneficial, it is acknowledged that it will give rise to significant difficulties including issues associated with the tracing of the income.
- Accordingly it is submitted that a CGT exemption exist in relation to the sale of shares in Australian owned overseas companies which are carrying on an active business. Rules which have been implemented in the UK could be used as a guide for such legislation. It will also be necessary to ensure that the profit arising from such sales can be paid to the ultimate overseas shareholder free from withholding tax.

CFC RULES

- The CFC rules contained in Australia's tax legislation are arguably the most complex area of Australian tax law.
- The "band-aid approach" of rectifying perceived anomalies and difficulties is only likely to add further complexity to these rules.
- There are a number of examples (including the UK) of simpler CFC rules operating efficiently.
- The Australian CFC rules do not, according to Treasury figures, generate significant tax revenue.
- Fundamentally the CFC rules should seek to attribute passive income which is derived in low tax jurisdictions. It is submitted that this can be achieved through the introduction of less complex legislation.
- Accordingly it is submitted that the CFC rules should be redrafted taking into account the overall purpose of the provisions and having regard to similar legislation which exists in other jurisdictions.

DOUBLE TAX AGREEMENTS

- Many of Australia's Double Tax Agreements which apply to our major trading partners reflect a previous era of economic activity.
- The free flow of capital and investment returns can be influenced by the provisions of the Double Tax Agreements.
- The modernization of Australia's treaties with its major trading partners must be a priority for Treasury.
- It is submitted that Double Tax Agreements should entrench into Australia, international initiatives to reduce the impact of withholding tax and eliminate the impost of taxes on capital gains derived by our major trading partners.
- Treasury should be encouraged to seek external consultation as part of the process of treaty negotiations.

DUAL RESIDENT COMPANIES

- The concept of residence is fundamental to Australia's tax regime and therefore any change needs to be approached with caution.
- Proscribing the tax residence of dual resident companies could have significant adverse tax implications.
- It is submitted that "grand fathering rules" will need to accompany the introduction of such a change.

TAX ON THE SALE OF NON-RESIDENT INTERPOSED ENTITIES

- There is a proposal which suggests Australia should seek to tax (in some way) the profit arising from the sale of shares in a non-resident interposed entity by a non-resident entity in circumstances where the interposed entity holds shares in an Australian resident entity.
- Having regard to the comments made in relation to the context of the proposed reform it is apparent that this proposal is counter productive to a move towards greater freedom of capital and investment flows into Australia.
- It is submitted that this proposal should not be pursued.