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Office of Chief Financial Officer

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The International Taxation Project
Board of Taxation Secretariat
C/- The Treasury
Langton Crescent
PARKES ACT 2600

Dear Sir

REVIEW OF INTERNATIONAL TAXATION ARRANGEMENTS (RITA)

BHP Billiton welcomes the Government's initiative in commencing RITA and particularly welcomes the involvement of the Board of Taxation in the consultation process. In response to RITA, BHP Billiton takes this opportunity to comment on issues raised in the Consultation Paper. BHP Billiton is lodging, with the Secretariat, a joint submission with a number of other large Australian publicly listed entities in regard to Chapter 2 and various matters raised in Chapter 3. BHP Billiton has also reviewed the joint BCA/CTA submission and generally concurs with the views expressed in that submission.

BHP Billiton's views on tax reform continue to be predicated on growing the business and shareholder value in an increasingly competitive globalised market and uncertain investment outlook. It is, in our view, important that the options under consideration actively encourage future business activity, reduce the cost of doing business, and lead to a more internationally competitive Australian taxation system.

Against this background, we note that the Consultation Paper does not include a set of objectives in regard to RITA. We have set out below, the objectives, which we believe, should be the cornerstone of the review and final recommendations should be tested against these objectives with a view to improved outcomes. These objectives are as follows;

1. Encourage Australian companies to invest offshore;
2. Encourage foreign investors to invest in Australia companies;
3. Domestic investors to be neutral between investing in domestic companies with only Australian based activities versus domestic companies with foreign based activities;
4. Encourage foreign companies to locate parent or regional parent companies in Australia. Encourage foreign ownership of assets under Australian companies;
5. Australia to levy tax only on passive (e.g. interest, royalties etc) foreign income earned in unlisted countries.

Our other comments specifically in regard to the Consultation Paper are outlined below.

Chapter 2 - Attracting Equity Capital For Offshore Expansion

The current law in regard to the taxation of foreign source income by Australian companies contains a bias which discourages such foreign investment, by imposing further Australian tax on the profits distributed to shareholders, and not recognising the underlying foreign tax already paid upon the profits. To eliminate this bias companies should be able to pass the benefit of foreign tax paid on foreign profits on to resident shareholder or non resident shareholders i.e.; streaming to avoid or reduce the imposition of double taxation on foreign profits. This double taxation is simply illustrated;

	Foreign	Domestic
Profits	$100	$100
Foreign Tax (30%)	$30	Nil
Foreign Withholding Tax (15% of dividend)	$10.50	Nil
Australian Company Tax	Nil	$30
Australian Shareholder Tax (48.5%)	$29	$18.50
Total Tax	$69.50	$48.50
After tax return	$30.50	$51.50

The removal of this double taxation of foreign income or bias away from foreign income could be achieved by providing domestic shareholder relief for unfranked dividends paid out of foreign profits (Option 2.1A). However, the relief should be at a rate of 3/7 for profits sourced from Broad Exemption List Countries ("BELC") and up to 3/7 but limited to underlying tax paid for income earned in non-BELC countries. The detailed analysis is included in the abovementioned joint submission, but is summarised as follows;

1. The foreign dividend account system would be converted into a tax-paid system (as was recently done with the imputation system).
2. An Australian company would be entitled to a credit in its foreign dividend account when it receives a non-portfolio dividend from a foreign company. The credit would correspond to the amount of foreign tax on the dividend and the profits from which it was paid. However, the credit would be limited to the Australian tax that would have been imposed on those profits in a domestic context (i.e. $\frac{3}{7}$ of the dividend). In the case of a dividend received from a company in a BELC or from domestic income of a company in a limited-exemption listed country the credit would be granted automatically at the maximum rate (reflecting the assumption that the underlying profits have already been comparably taxed).
3. An Australian company would be entitled to frank a dividend from its franking account and/or foreign dividend account (at its option).
4. A non-resident shareholder that receives a dividend that is franked from the franking account or foreign dividend account would be exempt from withholding tax (as at present).
5. A resident shareholder who receives a dividend that is franked from the franking account would gross-up the dividend for the credit, calculate tax at their marginal rate and then offset the credit against their tax liability (as at present). If the credit exceeds the Australian tax on the dividend then the excess can be offset against tax on other income or refunded (also as at present).

6. A resident shareholder who receives a dividend that is franked from the foreign dividend account would gross-up the dividend for the credit, calculate tax at their marginal rate and then offset the credit against their tax liability. However, unlike dividends franked from the franking account, the foreign dividend account credit will be limited to the actual Australian tax on the dividend income and no refunds will be given for excess credits.

However, for integrity and simplicity purposes, the following additional features would be included;

- The foreign dividend account credit would be limited to the Australian company tax rate. Foreign tax payments would therefore not have full value if the effective foreign tax rate on the dividend income exceeds the Australian company tax rate;
- Foreign dividend account credits could not be offset against Australian tax on other income. Foreign tax payments would therefore not have full value if the shareholder's Australian tax rate is less than the company tax rate; and
- Foreign dividend account credits could not be refunded if they exceed the Australian tax on the shareholder's income. Foreign tax payments would therefore not have full value if the shareholder's Australian tax rate is less than the company tax rate and they have no other income.

Chapter 3 - Promoting Australia as a location for Internationally focussed Companies

The Controlled Foreign Company (CFC) rules should be limited to their original policy intent and only tax passive income in tax havens, which would also have the added benefits of simplifying the existing rules and significantly reducing compliance costs. This would not require a complete rewrite of the CFC provisions but rather 3 key amendments to the existing law;

1. Remove companies operating in Broad Exemption Listed Countries (BELCs) and all underlying investments from the operation of the CFC rules, in conjunction with a review of which countries are included on the BELC list (Option 3.3);
2. Provide a general exemption for all foreign non-portfolio dividends received by Australian companies (Option 3.9); and
3. Redefine the scope of "passive" income to exclude "tainted services" such that income from an active business, albeit via the provision of services, is not subject to attribution (Option 3.2).

BHP Billiton recommends the test for company residency be based on incorporation, which is far more appropriate in today's globalised environment. The option to consider the residency test based upon effective management is too narrow, impractical in today's business world with its various electronic communication mediums and should be considered in a broader context.

BHP Billiton recommends that the dividend exemption (discussed above at point 2) should be supported by an exemption from capital gains tax for capital gains from the sale of non-portfolio interests in foreign companies consistent with developments in Europe and most recently the UK. This would harmonise the treatment of dividend income with the treatment of capital gains resulting from the sale of a foreign company that has retained profits. However, we would not propose to grant a foreign dividend account credit in respect of such capital gains (except to the extent they arise from the sale of a company in a BELC or have actually been taxed in a foreign country).

Chapter 5 - Improving Australia's Tax Treatment of Foreign Expatriates

The proposed security deposit for residents departing Australia should be abandoned. More fundamentally, a current law in regard to the deemed disposal of assets at the time of cessation of Australian residency in regard to assets at the time of commencing Australian residency should be repealed. BHP Billiton has made a number of submissions to Government in regard to this matter, as, in our view, the Government's proposed solution of addressing the issue via Treaty renegotiation does not properly address the issue. Refer attached submissions to Government.

Consistent with the matter above, the proposal to treat a cessation of residency as a "cessation event" for the purposes of Division 13A be abandoned.

Furthermore, Australia should only have taxing rights in regard to employee share plans to the extent any discount is sourced in Australia. This is consistent with the proposals contained in TLAB 4, which we understand is to be reintroduced as TLAB 7. The source of the discount should be determined via a pro-rata calculation of Australian workdays. (This is consistent with OECD views re the taxation of employee share plans). As an adjunct and to avoid the potential double taxation of employee share options, amendments should be sought to Treaties to avoid double taxation that may arise due to different taxing methods in a foreign jurisdiction.

We would welcome the opportunity to further participate in the consultation process and discuss this or our joint submission in any further detail. Should your require any further information or details, please do not hesitate to contact Ian Edney on 03 9609 3997.

Yours faithfully,

Chris Lynch
Chief Financial Officer