



# Guidance Note 12

## Tax Conditions

- Foreign investment is important, but it must work in Australia’s national interest. The impact of tax risks in foreign investment proposals on Australian tax revenue is a key consideration of the national interest test.
- The Government is increasing scrutiny of tax arrangements which pose a risk to revenue to ensure that multinational companies are adhering to Australia’s taxation laws. The Government’s approach to tax risk reflects the international trend to ensure that entities pay the right amount of tax in the countries in which they operate and where value creation occurs.
- Additional scrutiny, and tax conditions where necessary, will be applied to foreign investment proposals with certain tax risk characteristics particularly those assessed as medium or high risk.
- If a foreign investment proposal is approved, it may be approved subject to certain conditions, including tax conditions.
  - A set of guiding principles have been established to aid in the development of any condition(s). See the *Principles for Developing Conditions* Guidance Note.
- The Government will take appropriate and proportionate action to mitigate identified tax risks through the use of tax conditions:
  - The Treasurer will impose tax conditions to an investment where they are considered necessary to protect the national interest. This will be done on a case-by-case basis and may be tailored to significant or particular tax risks.
- Maintaining strong compliance with Australia’s foreign investment legislation is a priority for the Government. Failure to comply with Australia’s foreign investment legislation – including tax conditions – can result in significant penalties, including enforceable undertakings, direction orders, infringement notices, civil and criminal penalties.



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## A: Tax risk assessment

Treasury and the Australian Taxation Office (the **ATO**) work closely together to assess foreign investment proposals and provide advice to the Treasurer. The ATO has a dedicated Tax Consult area that is consulted on foreign investment proposals to assist the Treasurer in making a decision as to whether an action is contrary to the national interest.

Separately, the ATO also has a dedicated foreign investment screening team that administers the *Foreign Acquisitions and Takeovers Act 1975* (the **Act**) with respect to screening of foreign investment proposals in residential land. The ATO's foreign investment screening team may consult with the ATO Tax Consult area on these proposals if considered necessary. The ATO's foreign investment screening team is separate from the ATO's Tax Consult area with whom it consults.

The scope of the ATO's Tax Consult advice about an action is the potential impact on the Australian Government's tax revenues and the integrity of the federal tax system. The ATO Tax Consult advice provides a risk rating of 'low', 'medium' or 'high' for each action along with qualitative advice on the risks to tax revenues and the integrity of the tax system as a result of the action. The following risk rating definitions are adopted:

- Low: the ATO has not identified significant tax issues.
- Medium: there may be a risk to tax revenue or to the integrity of the tax system.
- High: there is a clear risk to tax revenue or to the integrity of the tax system.

One distinguishing factor between risk ratings of 'medium' or 'high' is the likelihood of the outcome occurring. High risk ratings indicate that the estimated tax consequence of the action is 'likely' to occur rather than it being just 'possible'.

The ATO may assess an action that involves complex structuring (such as layered trusts or the use of holding entities in low or no tax jurisdictions) as low risk if that structuring does not create Australian tax issues of concern.

The ATO's Tax Consult advice is confidential to Treasury. Applicants who are proposing to take an action(s) assessed as High risk will generally be:

- Notified of their High risk rating;
- Subject to tax conditions; and/or
- Subject to follow up or review by the ATO following completion of any proposed action(s).

## B: Summary of tax issues

The ATO's advice to the Treasurer and risk rating may reflect a broad range of matters including:

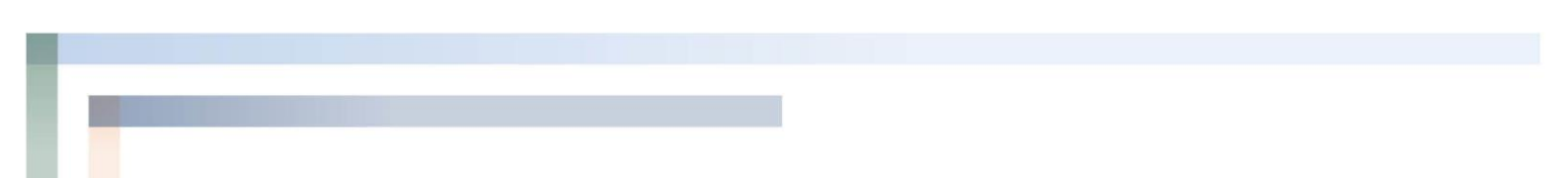
- Compliance with the substantive tax law;
- The tax compliance history of the investor and its related parties;
- The transparency of the investor's engagement with the ATO;
- The choices and behaviours that the investor evidences in their tax affairs;
- Potential application of the general anti-avoidance rule and the Diverted Profits Tax;
- Tax outcomes that are inconsistent with the policy intent of tax laws;
- Maintaining the integrity of the tax regime;
- Related or earlier actions undertaken that are relevant to the consideration of the proposal;
- Tax collection risk on disposal by the investor or vendor; and
- Whether the arrangement has features of concern, or is within high-risk parameters identified by the ATO in guidance material including, but not limited to:
  - Taxpayer Alerts;
  - Practical Compliance Guides;
  - ATO Interpretative Decisions; and
  - Tax Rulings.

The ATO's [legal database](#) sets out a complete list of public guidance.

### Specific tax issues of interest

Additional scrutiny will be applied to foreign investment proposals with certain tax characteristics likely to be considered higher risk. The following are examples of arrangements that will attract the ATO's attention:

- Internal reorganisations or other intragroup transactions which may represent initial steps of a planned Australian tax avoidance arrangement, for example:
  - Inversions designed to facilitate subsequent profit shifting.
  - Avoidance of capital gains tax by contrived use of the multiple entry consolidated group rules.
  - Debt creation in connection with funding related party transactions (noting possible interactions with Australia's thin capitalisation rules).
  - Migration of intangibles designed to reduce or avoid Australian taxable income and or reduce royalty withholding tax.
  - Structuring designed to avoid income being attributable to an Australian permanent establishment.

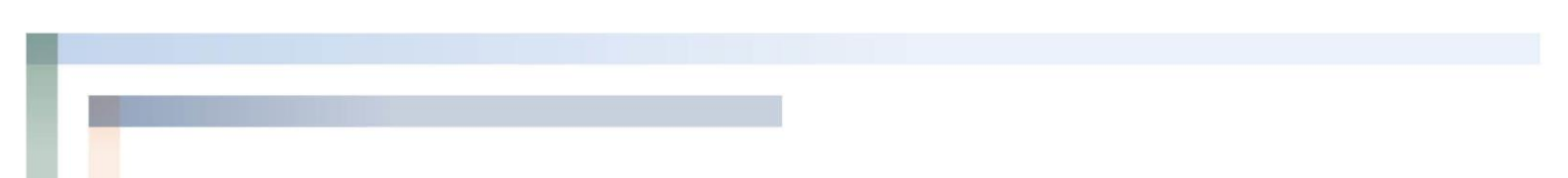
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- Structuring arrangements in order to obtain the benefit of a reduced withholding tax rate.
  - Related party financing arrangements that:
    - Artificially defer or avoid interest withholding tax while obtaining annual Australian income tax deductions.
    - Avoid or reduce dividend withholding tax upon repayment/redemption of related party financing arrangements.
    - Adopt an excessive interest rate and/or amount of debt so as to reduce taxable income.
    - Disguise the use of financial arrangements to make or facilitate transactions with, or payments or distributions to, related parties (noting possible interactions with Australia’s thin capitalisation rules).
  - Replacement of a foreign inbound holding structure, covered by the imported hybrid mismatch rules, with a different structure to obtain more favourable Australian tax outcomes under the hybrid mismatch provisions.
  - Investments that are structured through effective low or no tax jurisdictions where there is limited relevant economic activity taking place.
  - A transaction that otherwise has one or more of the following features:
    - Appears to make no commercial sense.
    - Appears overly complex or convoluted.
    - Involves hybrid financing instruments which appear designed to obtain more favourable Australian tax outcomes under the hybrid mismatch provisions.

## Related or earlier actions undertaken

The ATO undertakes a broad and holistic examination of the circumstances surrounding each action and each investor (including the circumstances of the vendor where necessary). In formulating its advice about the impact of an action on the Australian Government’s tax revenues, the ATO considers:

- The tax impact of earlier transactions undertaken by the investor and its related parties;
- Any patterns of behaviour by the investor and its related parties;
- Any pre-existing arrangements that may affect the tax revenue from the proposed action; and
- Known future actions that are related to the action and that may affect the tax revenues from the action, including elements that may occur entirely offshore.

For example, if asked to consider the tax risk associated with the acquisition of a new asset by an investor, the ATO may have regard to any related party financing arrangements already in place that may have the effect of reducing the tax payable in respect of income to be derived from the new asset. This may be especially relevant when the ATO is asked to advise on the tax



impact of a proposals for an exemption certificate, which allows an investor to take certain actions (for example, acquisition of multiple unspecified land titles) over a period of time.

### **If the applicant is unable to provide sufficient information**

The Treasury and ATO require that all relevant information specified in the Proposal Checklist (including Appendix – Tax Checklist) be provided with the proposal.

If an applicant is unable to provide any of the requested information, they should provide comments as to the reasons why. In these cases, there may still be a possibility of the tax risk being assessed by the ATO as either ‘low’ or ‘medium’ depending on the nature of the potential risks.

If the information is not available at the time of providing a response, but is expected to become available later, the applicant should:

- Provide a timeframe within which the information will (or is expected to) become available, and
- Provide that information, and any other relevant information, when it becomes available.

Where information is not provided as part of the initial submission, it will routinely be subsequently requested through a request for information which will contribute to an extended review time for the proposal. In some cases, the ATO may require further additional information (not specified in the Tax Checklist) to better understand the proposed transaction and the potential tax risk.

If information is requested through a request for information and is unable to be supplied, the ATO may recommend that the decision-maker impose additional tax conditions including requiring the applicant to provide the information later.

## C: When may a tax condition be imposed?

See also the *Principles for Developing Conditions* Guidance Note.

### Provision of information generally

Under the Act and taxation law, the Treasury and the ATO respectively can require foreign investors to provide documents or information within specified timeframes. This may be done before or after investors have taken action(s) regardless of whether they were assessed as low, medium or high risk in relation to Australia's tax revenue or to the integrity of the tax system.

### Tax conditions

If, following consultation, the Treasurer considers that tax conditions need to be applied to protect the national interest (including to address a risk to the integrity of the tax system and/or tax revenue), conditions may be imposed as part of a no objection notification or exemption certificate, to ensure that an action will not be, or is not, contrary to the national interest.

The imposition of tax conditions will be done on a case-by-case basis, and any conditions would be tailored to the circumstances of the action under consideration. This may occur where the relevant action(s) has been assessed as medium or high risk.

Investors will be given an opportunity to review and respond to proposed conditions as part of the procedural fairness process.

In cases where particularly complex or novel conditions are proposed, or the investor considers that there is an error or other technical issue with the proposed conditions, the investor may ask to discuss this further with the Treasury, or jointly with the Treasury and the ATO. Both Treasury and the ATO are willing to engage in such discussions with investors, where appropriate.

Should an investor wish to request such a discussion with either the Treasury, or jointly with the Treasury and the ATO, they can ask for this when responding to the procedural fairness process. All engagement with the ATO should be initiated through the Treasury.

It is important that all representatives for the investor are appropriately authorised to talk to both the Treasury and the ATO prior to any discussions taking place. In respect of discussions involving the ATO, if an adviser is not the registered tax agent of the investor it is recommended anyone involved in the discussion is authorised prior to any discussion. Details regarding the process for authorising representatives are available on the [ATO website](#).

## D: Examples of tax conditions<sup>1</sup>

In complying with the tax condition(s) imposed in a no objection notice or exemption certificate, where appropriate, the Applicant can claim that the documents are protected from production by legal professional privilege or an administrative concession granted by the Commissioner of Taxation. Any claims for privilege or concession should be made in a timely manner. It is expected that the Applicant and entities within its control group will act consistently with the relevant ATO guidelines. [Compliance with formal notices – claiming legal professional privilege in response to formal notices – Legal professional privilege \(LPP\) protocol](#) contains the ATO's recommended approach for identifying communications covered by legal professional privilege and making legal professional privilege claims to the ATO.

This section gives a non-exhaustive guide about the information which may be required under tax conditions.

Investors should note that conditions are recommended based on particular circumstances, and will be considered on a case-by-case basis.

### General

A general tax condition may require the investor to provide the following information to Treasury ([foreigninvestmentcompliance@treasury.gov.au](mailto:foreigninvestmentcompliance@treasury.gov.au)) and ATO ([ATO-FIRBS@ato.gov.au](mailto:ATO-FIRBS@ato.gov.au)) within 90 days of the transaction completing:

- Where a new Australian entity associated with the transaction(s) has been incorporated, the Tax File Number (TFN) or Australian Business Number (ABN).
- The details (name, position and firm) and engagement letter(s) of any lawyer/s and/or tax adviser/s who advised on Australian tax matters in relation to the proposed acquisition(s), Foreign Investment proposal and/or request for information/condition response.
- Most recent audited financial statements for the Target Entity/Entities, or, if audited financial statements are not available, the latest financial records or unaudited financial statements.
- Detail any changes to the structure diagram in the proposal cover letter and the final structure (including any interposed entities).
- Detail any steps in the transaction(s) which have not been implemented and the reasons why.
- Up-to-date information in relation to the action(s), including any changes upon implementation in comparison to the action(s) in the foreign investment proposal.
- Confirmation of when the transaction(s) is implemented and if the transaction has been implemented as advised.

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<sup>1</sup> The Treasurer has the power to impose any condition(s) that the Treasurer considers necessary to protect the national interest (or national security, as the case applies). While this section of the *Guidance Note* outlines some of the more common tax conditions applied, all investments are considered on a case-by-case basis, and therefore the actual conditions imposed may vary from these.



- Whether any part of the proposed acquisition(s) has features or an arrangement covered by one or more Taxpayer Alert(s) issued by the ATO<sup>2</sup>. Taxpayer alerts can be found on the ATO legal database.

### Provision of information

Where a proposed acquisition raises tax risk issues and there is insufficient information to assess the proposal, conditions may require the Applicant to provide any documents or information<sup>3</sup> that is reasonably required to be provided to the ATO. This includes documents or information in accordance with the taxation laws of Australia in relation to the action(s), and any transactions, operations or assets in connection with assets or operations acquired as a result of the action(s).

The Applicant would be required to:

- Provide the information within the timeframe specified by the ATO unless otherwise agreed;
- Ensure complete and up to date information is provided in relation to the action(s);
- Advise on any changes to the proposal upon implementation; and
- Confirm when the transaction(s) is implemented and if implemented as advised.

The Applicant would also be required to use its best endeavours to ensure, and within its powers ensure, that entities in its control group comply with equivalent requirements.

### Restructures / Reorganisations

Where a proposed acquisition contains steps that form part of, or are in connection with, a broader global restructure or reorganisation, conditions may require provision of diagrams and details about global steps including:

- Pre and post transactions and structures.
- Flow of funds.
- Management and/or tax residency of parties to the steps.
- Details of the tax consequences of the steps.

### Thin Capitalisation

Where a proposed acquisition involves an entity that is subject to the thin capitalisation rules, conditions may require provision of the following:

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- 2 As required by Category C of the ATO's reportable tax positions, applicants must disclose arrangements that have characteristics of taxpayer alerts, even if some features of the proposed arrangement are different to those described in the alert, or the arrangement is not viewed by the applicant or their advisers as aggressive, contrived or artificial.
  - 3 This includes documents or information held, possessed or stored outside Australia.

- Details of that entity's choice of method (for the income year in which the action arises) for the purpose of determining their respective earnings limit or maximum allowable debt, including information that clarifies circumstances and arrangements relevant to that entity's choice.
- Where related party debt has been issued as part of the acquisition, information relating to the use of the related party debt. This includes information such as related party payments and transactions.
- Where there is an allocation of third-party debt to an Australian entity in the context of a global acquisition, information relating to the use of the third party debt in Australia.

### Financing

Where a proposed acquisition involves related party debt financing, conditions may require provision of the following:

- Details of counterparties, key terms and conditions, legal characterisation, tax treatment (e.g., treatment under Division 974 of the *Income Tax Assessment Act 1997*).
- Transfer pricing documentation.
- Australian and overseas tax treatment of any distribution or interest payment made by an Australian entity to an investor or non-resident associate after the proposed acquisition.
- Details of any associated related party derivative arrangements.

### Private Equity / Private Capital

Where the applicant(s) is a Private Equity fund, conditions may require provision of the following:

- Details relating to the disposal and the Australian tax consequences arising from the disposal.
- The applicant to engage with the ATO prior to any disposal of the interest resulting from the action.

### Conditions Reporting

Where there are ongoing concerns with a proposed action(s), the Applicant may be subject to a 'Conditions Reporting' condition as per below:

- The Applicant must provide an annual report to the Government on compliance with its tax conditions. In the response, the Applicant must provide the Australian Company Number and/or the ABN of the Australian entity/ies used for the proposed transaction where available.
- The first report must cover the period from the date the action(s) takes place to the end of the Applicant's income year for tax purposes. If the action takes place less than 90 days before the end of the first income year, then that period can be incorporated in the next report. All subsequent reports must cover the Applicant's income year for tax purposes. Each report must be provided by the due date for lodgement of the Applicant's tax return for that year.

- The Applicant's obligation to lodge annual reports will be terminated where the Applicant has lodged 3 annual reports since the relevant action(s) has been completed. Where the Applicant proposes to undertake a program of actions, then the obligation will be terminated on lodgement of 3 annual reports after the final action. The termination of this condition does not change the Applicant's obligations under other conditions which may be in effect.

Further information on reporting to the Government on compliance with conditions can be found in the *Conditions Reporting* Guidance Note.

The Treasurer may also request the ATO's view of whether, or to what extent, the Applicant has satisfied its condition reporting including how effectively documents or information are being provided to the ATO.

## E: What is the effect of the conditions?

In response to particular tax risks some conditions may impose specific obligations. These may include requiring the investor (and/or its associates) to supply certain information, notify the ATO of certain events, to engage with the ATO about particular risks, to enter into good faith negotiations with the ATO or to take other action to resolve tax issues. These may not necessarily be required to be completed in order for a no objection notification or exemption certificate to be given, but may be required within a certain timeframe after the transaction being undertaken.

Regardless of whether any conditions are imposed, all obligations under Australian tax law must be met.

## F: Consequences of non-compliance with conditions

Conditions imposed on foreign investors as part of a no objection notification or exemption certificate are legally binding and must be complied with.

Maintaining strong compliance with Australia's foreign investment legislation is a priority for the Government. Failure to comply with Australia's foreign investment legislation – including tax conditions – can result in significant penalties, including enforceable undertakings, direction orders, infringement notices, civil and criminal penalties. The ATO and Treasury work together and share information to carry out their roles as administrators of Australian taxation laws and the foreign investment framework respectively.

## G: Further information

### Providing documents or information requested by the ATO

To ensure that an action does not give rise to or have ongoing tax issues that would make it contrary to the national interest, conditions may require that information that is reasonably requested by the ATO, including in accordance with the taxation laws of Australia, must be provided to the ATO within the timeframe specified by the ATO.

Compliance with conditions does not require the investor to waive any common law or statutory rights or privileges, or the accountant's concession as provided in the ATO's access guidelines.

Conditions may extend to the investor making best endeavours to ensure that the investor's control group also provides information as is reasonably requested by the ATO including in accordance with the taxation laws of Australia.

See below for the meaning of 'control group' and 'best endeavours.'

### Meaning of control group and best endeavours

#### Control group

A control group consists of entities that: control the Applicant (a controller); any entities that a controller controls; and that the Applicant controls, which includes for the purposes of these conditions an entity that is the subject of the proposal.

Control for this purpose is defined in section 50AA of the *Corporations Act 2001*. Section 50AA refers to the capacity to determine the outcome of decisions about another entity's financial and operating policies. It considers practical influence (rather than the rights that can be enforced) and practices or patterns of behaviour. It excludes circumstances where an entity has the capacity to influence decisions about another entity's financial and operating policies but is under a legal obligation to exercise that capacity for the benefit of someone other than its own members.

#### Best endeavours and within its powers

If an investor controls another entity as per the definition of section 50AA of the *Corporations Act 2001*, then it would generally be expected that it is within the investor's powers to ensure that the other entity acts in accordance with the condition applied.

For an entity in the investor's control group that the investor does not control, the investor is expected to use its best endeavours to ensure that the other entity acts in accordance with the relevant condition.

Depending on the circumstances this might involve making representations to that entity and the controlling entity in relation to the relevant conditions in person and/or in writing. Best endeavours means to do all one reasonably can and this will depend on the relationships between the entities, the conditions that have been applied and the particular circumstances.



## H: Tax risk notification paragraphs

Tax risk notification paragraphs (**TRNPs**) serve to alert investors to particular tax risks that the ATO has identified that may warrant their consideration. TRNPs often request that the investor engage with the ATO to discuss the identified issues further.

TRNPs are not conditions imposed upon investors and are therefore not legally binding. Where the ATO has reason to suspect that an investor may not be willing to engage voluntarily with the ATO, and the ATO believes such engagement is necessary to mitigate tax risks, the ATO may recommend that this requirement be imposed via a legally binding tax condition.



## Further information

Further information is available on the [Foreign Investment website](#) or by contacting 1800 050 377 from Australia or +61 2 6216 1111 from overseas.

**Important notice:** This Guidance Note provides a summary of the relevant law. As this Note tries to avoid legal language wherever possible it may include some generalisations about the law. Some provisions of the law referred to have exceptions or important qualifications, not all of which may be described here. The Commonwealth does not guarantee the accuracy, currency or completeness of any information contained in this document and will not accept responsibility for any loss caused by reliance on it. Your particular circumstances must be taken into account when determining how the law applies to you. This Guidance Note is therefore not a substitute for obtaining your own legal advice.