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# Australia proposes GAAR reforms to address tax avoidance

February 27, 2013

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## ***In brief***

The Australian government on February 13 introduced draft amendments to the Australian general antiavoidance rules (GAAR, commonly referred to as Part IVA). The GAAR is designed to protect the integrity of Australia's income tax system. The amendments are intended to counter schemes that technically comply with the requirements of the Australian law but, when viewed objectively, may be conducted to avoid tax.

If approved by the Australian Parliament in their current form, the proposed amendments would apply retroactively to all entities that entered into or commenced to carry out any transaction, acquisition, or restructuring involving Australia, whether directly or indirectly, on or after November 16, 2012.

US multinationals with existing or planned operations or investments in Australia should consider how these amendments could affect active investment structures or transactions undertaken on or after the proposed effective date.

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## ***In detail***

The current Australian GAAR prevents taxpayers from obtaining any Australian income tax benefit arising from a scheme where the Commissioner of Taxation is able to establish the existence of:

1. a scheme, which is broadly defined under the tax legislation as any arrangement, plan, proposal, action, course of action or contact, whether unilateral or otherwise.
2. an Australian income tax benefit ('tax benefit') resulting from the scheme, which involves comparing

the scheme's tax outcomes results from any alternative schemes that the taxpayer might reasonably be expected to have entered into, and

3. the sole or dominant purpose of being a party to the scheme is to obtain the scheme's tax benefit.

The government introduced the amendments in response to recent taxpayer victories in Federal Court cases on applying existing GAAR rules. In some of these cases, the taxpayers were able to argue successfully that they did not obtain a 'tax benefit' because, had they not entered into the particular

scheme, they would not have entered into another arrangement that attracted tax. That is, they would have entered into another scheme that would have given rise to the same tax outcomes, or done nothing at all.

## ***The proposed legislation***

The draft legislation would create two separate and distinct situations that would trigger application of Part IVA: the taxpayer obtains a tax benefit that either (1) would not or (2) might reasonably be expected not to have occurred if the scheme had not been entered into or carried out. If either

section is satisfied, Part IVA may be applied.

We expect that the first section would be applied only to aggressive tax schemes and a limited class of deduction cases in which the deduction arises only as a consequence of the scheme.

For the second section, the draft legislation introduces a set of parameters for the hypothetical reconstruction of events based on what might reasonably be expected to have occurred (the identification of an 'alternative scheme') for comparison under the tax benefit analysis. The Explanatory Memorandum to the draft legislation (EM) states that in identifying a reasonable alternative scheme for the purposes of this section, the alternative scheme should

achieve 'substantially' the same non-tax results as those achieved through the scheme. However, note that the EM also provides that the non-tax results should simply be 'comparable.'

The EM adds that the reference to 'non-tax' results merely excludes considerations of Australian income tax outcomes. Taxpayers could argue that the imposition of state taxes such as stamp duty or non-Australian taxes may be a compelling factor that makes an alternative scheme unreasonable.

**Note:** There are inconsistencies in the EM and the draft legislation that will need careful consideration and may be debated and considered by taxpayers, the Australian Tax Office, and the courts. However, while there will be questions on interpreting the new law,

the application of Part IVA in practice will depend largely on the specific facts and availability of evidence relevant to the alternative schemes identified and an objective inquiry into the dominant purpose of parties to the scheme.

### ***The takeaway***

Taxpayers that have entered into or began carrying out any transaction, acquisition, or restructuring on or after November 16, 2012, should consider how the proposed amendments would affect the transaction. Taxpayers should also document the commercial drivers (including non-Australian income tax reasons) for undertaking any step that may give rise to a tax-efficient Australian income tax outcome.

### ***Let's talk***

For a deeper discussion, please contact:

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