Private Wealth International Program

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About the program

The Private Wealth (PW) International Program supports the Tax Avoidance Taskforce through engaging with privately owned and wealthy groups that have international operations and dealings. The Program seeks to give the community confidence that privately owned groups are paying the right amount of tax.

Our program delivers a combination of approaches to help you understand and comply with your tax obligations, including:

- education campaigns to raise awareness about new measures or guidance
- developing public advice and guidance on international tax
- partnering with you through early engagement activities to provide certainty on significant transactions and events
- targeted risk campaigns, risk-based reviews, and audits where appropriate, based on risk assessments from a wide range of internal and external data sources.

As part of the program, we're also providing input to relevant new international tax measures affecting private groups.

For information about other PW programs, see:

- Tax performance programs for privately owned and wealthy groups
- Commercial deals program
- Tax Avoidance Taskforce – Trusts
- Promoters and Tax Exploitation Program

Our population

Our population includes all privately owned and wealthy groups that engage in international dealings including those that are covered by the Top 500, Next 5,000, and Medium and Emerging tax performance programs.

We provide dedicated support to the tax performance programs to identify and address international risks. We also collaborate with stakeholders across the ATO to ensure international risks are treated consistently.

International risks that we're focused on

Our program focuses on treating the following key international tax risks:

- related party financing risk
- intangibles migration
- controlled foreign companies (CFC)
- non-resident withholding tax
- tax residency (both individual and corporate)
- related party service arrangements.

There are other international issues that also attract our attention. For more information, see International transactions.

In some cases, we have also observed poor record-keeping, reporting and lodgment practices. To learn about your record-keeping requirements, see Overview of record-keeping rules for business.

If you have international operations and transactions, you should consider if these dealings satisfy the definition of international related party dealings. If so, you must consider if you're required to lodge the international dealings schedule (IDS). See who must complete an IDS for circumstances that an IDS must be lodged. Refer to Forms and instructions for the relevant income year to help you complete the IDS.

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Related party financing risk

Related party financing risk can arise if you engage in cross-border financing arrangements.

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Related party financing (RPF) refers to financing arrangements (such as a loan) between related parties or associates. Our program focuses on PW taxpayers engaging in cross-border financing arrangements to achieve a tax benefit.

For example:

- related party financing arrangements which adopt non-arm’s length terms and conditions resulting in excessive debt deductions, particularly for property investment or development – see **Inbound related party financing for private groups in property and construction**
- claiming interest deductions on your related party loan, whilst failing to pay, credit or regularly capitalise interest amounts, resulting in the deferral or non-payment of interest withholding tax.

Other issues we commonly observe with cross-border related party financing arrangements include:

- debt versus equity characterisation (for example, interest-free loans)
- purported interest deductions on interest that is accrued and never paid
- outbound funding provided to overseas related parties on non-arm's length terms (for example, interest-free loans)
- the deferral or avoidance of income recognition in Australia
- use of purported loans to disguise foreign income or wealth in order to avoid assessment of offshore monies received by Australian resident taxpayers – see **Taxpayer Alert TA 2021/2** *Disguising undeclared foreign income as gifts or loans from related overseas entities*
- the deductibility of interest under section 8-1 or TOFA (taxation of financial arrangements) – see **Taxation of financial arrangements (TOFA)**
- non-lodgment of annual PAYG withholding from interest, dividend and royalty payments paid to non-residents reports
- thin capitalisation
  - incorrectly applying the $2 million de minimis exemption threshold, which should be calculated on an associate inclusive basis
  - compliance with safe harbour test (applicable before 30 June 2023)

- inappropriate use of arm's length debt test (prior to its repeal).

For income years starting on or after 1 July 2023, new thin capitalisation rules apply as part of the Treasury Law Amendment (Making Multinationals Pay Their Fair Share – Integrity and Transparency) Act 2024.

We have resources available to help you. For more information, see:

- **Inbound related party financing for private groups in property and construction** to learn about what to consider from a transfer pricing perspective if you have an inbound funding arrangement
- **Practical Compliance Guideline PCG 2017/4** *ATO compliance approach to taxation issues associated with cross-border related party financing arrangements and related transactions* to help you assess the risk of your related party financing arrangements
- **Characterisation of inbound foreign funds** to learn about cross-border arrangements that mischaracterise inbound foreign funds provided by non-residents to Australian taxpayers, covering inbound foreign funds of interest, foreign investors investing directly into businesses, loans and gifts and guidance on inbound foreign funds
- **Documenting genuine loans from related overseas entities** to learn about how to document your loan arrangements
- **Transfer pricing** to learn about the transfer pricing rules, including the arm’s length principle
- **Practical Compliance Guideline PCG 2017/2** *Simplified transfer pricing record-keeping options* for guidance on applying simplified record-keeping options and eligibility requirements for low-level inbound and low-level outbound loans
- **Thin capitalisation** for information about the rules and who is affected.

Inbound related-party financing for private groups in property and construction

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Intangibles migration

Intangible migration risk can arise if you have Australian-generated assets or rights.

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Intangibles migration refers to arrangements connected with the development, enhancement, maintenance, protection, and exploitation (DEMPE) of intangible assets, resulting in:

- disposal or migration of locally developed intangible assets (and associated future profit streams) to offshore jurisdictions on non-arm's length terms
- mischaracterisation and non-recognition of Australian activities connected with intangible assets held offshore
- mischaracterisation of payments to offshore entities in connection with intangible assets, such as the mischaracterisation of royalties as other types of payments (e.g. licence fees, service fees, tangible goods) to avoid withholding tax
- mispricing or non-recognition of arrangements relating to intangible assets to reduce tax liabilities.

We're concerned with privately owned and wealthy groups engaging in any transaction that allows an offshore party to access, hold, use, transfer or obtain benefits in connection with Australian-generated intangible assets or associated rights on non-arm's length terms.

For more information and other useful resources, see:

- Practical Compliance Guideline PCG 2024/1 *Intangibles migration arrangements* if you have an intangibles migration arrangement that involves an international related party, to self-assess the tax risk of your arrangement(s).
- Taxpayer Alert TA 2020/1 *Non-arm's length arrangements and schemes connected with the development, enhancement, maintenance, protection and exploitation of intangible assets*

provides a summary of our concerns regarding international arrangements that mischaracterise Australian activities connected with intangible assets.

- Taxpayer Alert **TA 2018/2** *Mischaracterisation of activities or payments in connection with intangible assets* provides a summary of our concerns regarding international arrangements that mischaracterise intangible assets or activities connected to intangible assets.

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Controlled foreign company

When the controlled foreign company provisions apply and risks we are concerned with.

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The controlled foreign company (CFC) provisions apply to Australian resident taxpayers with a substantial interest in a foreign company controlled by Australians.

The provisions operate to include a taxpayer's share of specified income and gains of a CFC in the taxpayer's assessable income. This is called attribution. Subject to some modifications, the income and gains of CFCs are worked out using the same tax rules that apply to residents.

We're concerned about:

- **non and under-reporting of attributable foreign income** by resident taxpayers
- tax returns and international dealings schedules being lodged with incomplete and inconsistent disclosures.

Information and examples to assist you in applying the CFC measures are available on our website in Chapter 1 of the **Foreign income return form guide**. In particular, it's important to understand these features:

- **Are you subject to the CFC measures?**
- **Does the CFC satisfy the active income test?**

- **Working out attributable income and the amount to include in your assessable income**

You can also refer to available summaries and worksheets to:

- **work out your control and attribution percentages**
- **work out the tainted income ratio for a CFC**
- **work out the attributable income of a CFC.**

Companies, partnerships and trusts who complete certain **trigger points** in their tax returns are required to complete the International dealings schedule. Instructions are available on how to complete **Section C: Interests in foreign entities** of the International dealings schedule.

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Non-resident withholding tax

The issues we've observed regarding non-resident withholding tax in privately owned and wealthy groups.

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When you make a payment of interest, dividend, royalty, or managed investment trust (MIT) payments to a non-resident, you may have an obligation to withhold tax. Withholding rates vary according to the type of payment, and whether the payee is a resident of a treaty country.

Issues that we've observed in privately owned and wealthy groups include:

- failure to lodge a **PAYG withholding from interest, dividend and royalty payments paid to non-residents – annual report** or an **annual investment income report**
- withholding tax hasn't been withheld or paid, or an incorrect amount is withheld or paid
- deductions for interest or royalty payments to an offshore entity are incorrectly claimed or misclassified on tax returns

- withholding tax exemption or tax treaty relief are incorrectly claimed
- inappropriate reliance on the exemption in **section 128F** or **section 128FA** of the ITAA 1936 to avoid liability to interest withholding tax – this includes where there was already an arrangement, agreement or understanding, that the debenture or debt interest would be issued to particular parties in a way that makes the offer not truly available to the public
- uncommercial arrangements where entities claim income tax deductions on an accruals basis but withholding tax isn't paid when deductions are claimed
- artificial structuring used to obtain a reduced withholding tax rate under a double-tax agreement
- artificial structuring and interposed offshore entities used to obtain a refund (in full or in part) of the withholding tax already withheld in Australia.

For more information on how the non-resident withholding tax mechanism works, refer to our guidance:

- **Investment income and royalties paid to foreign residents**
- **Interest, dividends, royalties, and MIT payments**
- **Who withholds**
- **When to withhold**
- **Withholding rate**
- **Obligations**
- Taxpayer Alert **TA 2018/4** *Accrual deductions and deferral or avoidance of withholding tax* provides a summary of our concerns regarding arrangements where income tax deductions are claimed on an accruals basis but withholding tax isn't paid when deductions are claimed.
- Taxpayer Alert **TA 2020/3** *Arrangements involving interposed offshore entities to avoid interest withholding tax* provides a summary of our concerns regarding arrangements that use offshore entities to avoid interest withholding tax.
- Taxpayer Alert **TA 2022/2** *Treaty shopping arrangements to obtain reduced withholding tax rates* provides a summary of our concerns

regarding arrangements designed to obtain the benefit of reduced withholding tax rates in relation to royalty or dividend payments from Australia. These arrangements may involve an interposed entity.

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Tax residency

It's essential to correctly assess tax residency to determine how an individual or entity will be taxed.

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Determining tax residency

Determining tax residency is essential in order to determine how an individual or entity will be taxed in Australia.

An Australian tax resident is assessable on their worldwide income, derived from all sources, for tax purposes. However, a non-resident is only taxed on their Australian-sourced income.

Due to the increasing globalisation of business and the global mobility of individuals, tax residency is a key risk in the privately owned and wealthy group market. Incorrect residency disclosures may lead to other tax risks, which may be present for the taxpayer and their wider group.

There's a small proportion of private group taxpayers that lodge their tax returns as non-residents for tax purposes. However, our data suggests that many of these could be residents.

Additional risks may arise because of a change in an individual or entity's tax residency status.

Individual tax residency

There are generally 2 scenarios where individuals may have incorrectly self-assessed as non-residents.

Individuals who remain Australian residents while overseas – individuals who are long-term Australian tax residents lodge as non-residents for income tax purposes while staying overseas. However, their facts and circumstances don't sufficiently demonstrate the cessation of their Australian tax residency.

Change of residency status for individuals entering Australia – individuals who visit and remain in Australia continue to lodge as non-residents despite their facts and circumstances demonstrating they're Australian tax residents.

Corporate tax residency

A company is a resident of Australia if either:

- it's incorporated in Australia, or
- it carries on business in Australia, even if not incorporated in Australia, and has either its
  - central management and control in Australia, or
  - voting power controlled by shareholders who are residents of Australia.

Corporate residency may also be affected by relevant tax treaties.

We have some tax rulings and guidelines to help determine individual and corporate residency.

- Taxation Ruling TR 2023/1 *Income tax: residency tests for individuals* outlines the residency tests for individuals for tax purposes and when a person will be considered as a tax resident of Australia.
- Taxation Ruling TR 2018/5 *Income tax: central management and control test of residency* provides how to apply the central management and control test of company residency.

- **Practical Compliance Guideline PCG 2018/9** *Central management and control test of residency: identifying where a company's central management and control is located* contains practical guidance to assist foreign incorporated companies and their advisors to apply the principles set out in Taxation Ruling TR 2018/5, to help determine whether they are a resident under the central management and control test of company residency.
- **Your tax residency** provides guidance on working out tax residency for individuals.
- **Working out your residency** helps business entities determine their tax residency.

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Related party service arrangements

What to consider if you have a related party service arrangement.

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If you are a member of a privately owned and wealthy group and you engage in related party service arrangements, you should consider the **transfer pricing** rules and the economic substance of your arrangement.

We are particularly concerned with the mischaracterisation of service arrangements where the legal form is inconsistent with the economic substance of the arrangement.

For example, where:

- individuals in Australia are performing activities for an overseas related entity that may be characterised as central management and control (CMAC) or key value-adding functions, but these activities have been mischaracterised as routine or low-value services. This may give rise to corporate residency risk or a transfer pricing benefit, and is typically more common where there's a concentration of control in a founder or director, or a small number of individuals in a privately held business.

- service fees are paid to an overseas related entity, but the benefit received by the Australian entity is questionable, or in some cases, the service wasn't provided at all. This may give rise to a transfer pricing benefit, particularly if the overseas service provider has no employees, and all activities are either performed by staff in Australia or outsourced to third-party providers that are directed by Australian staff.

For more information, see:

- Taxation Ruling TR 1999/1 *Income tax: international transfer pricing for intra-group services* – provides guidance on transfer pricing for intra-group services
- Practical Compliance Guideline PCG 2018/9 *Central management and control test of residency: identifying where a company's central management and control is located* – provides guidance on determining corporate tax residency of foreign incorporated companies under the central management and control test.

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New international tax measures affecting private groups

See new measures in international tax that may affect privately owned and wealthy groups.

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New thin capitalisation rules

The **Amending Australia's interest limitation (thin capitalisation) rules** is also known as the 'new thin capitalisation rules.' Changes were made to align with the Organisation for Economic Co-operation and Development's (OECD) Base Erosion and Profit Shifting (BEPS) Action 4. The new rules are now law and apply to income years starting on or after 1 July 2023. The debt deduction creation rules apply to income years starting on or after 1 July 2024.

The amendments apply to most multinational businesses operating in Australia, privately owned Australian entities that are foreign controlled, and to privately owned and wealthy groups with outbound operations. The de minimis threshold exemption continues to apply where debt deductions of all associate entities does not exceed $2 million for that year .

The old thin capitalisation rules continue to apply to Australian plantation forestry entities.

New tests for general class investors

Under the new rules, '**general class investors**' will be subject to one of 3 new tests.

Fixed ratio test

- an earnings-based ratio test that will limit an entity’s net debt deductions to 30% of its tax earnings before interest, taxes, depreciation, and amortisation (EBITDA)
  - debt deductions exceeding the 30% EBITDA limit will be denied
  - denied deductions can be carried forward for a maximum of 15 years (subject to the 30% EBITDA limit each year). This method is the default method unless a taxpayer makes a choice to use one of the other 2 methods.

Group ratio test

- an earnings-based worldwide gearing ratio test that will limit net debt deductions based on a ratio of the worldwide group’s net debt deductions and EBITDA based on the worldwide group's financial statements

- there is no carry forward of denied deductions under this method.

Third-party debt test

- an entity’s external (or third party) debt deductions, except for non-qualifying external debt deductions, will be allowed in full
  - debt deductions attributable to related parties are denied under this test
  - there is no carry forward of denied deductions under this method.

The arm's length debt test has been removed for all taxpayers.

Other considerations

Private groups including those with cross-border related party loans should also consider whether the terms and conditions of their arrangements, including interest rate and the amount of debt are arm's length under Australia's transfer pricing rules.

General class investors should also consider their approach when determining their remaining debt deductions for the purpose of applying the fixed ratio test or third-party debt test. This is because the previous transfer pricing limitation in section 815-140 (that an arm's length interest rate was applied to the actual amount of debt for thin capitalisation purposes) has been removed.

The new thin capitalisation rules are supported by the **debt deduction creation rules (DDCR)** that deny debt deductions arising from relevant related party loans to fund asset acquisitions, or prescribed payments such as distributions and returns of capital. The DDCR reduce the ability for multinational businesses and private groups, with at least $2 million in debt deductions (on an associate inclusive basis), to create debt through internal transactions.

The DDCR apply to income years starting on or after 1 July 2024 and apply to both existing and new domestic and international arrangements.

Complying Division 7A loans are not excluded from the operation of the DDCR.

More information

For more information and other useful resources, see:

- **Thin capitalisation rules** for information and guidance about the thin capitalisation rules and who they apply to.
- **Debt deduction creation rules and private groups** for a summary of DDCR and how they affect private groups.
- **Debt deduction creation rules and Division 7A** to learn about how DDCR applies and interaction with Division 7A.

Global and domestic minimum tax

On 9 May 2023, as part of the 2023–24 Budget, the Government announced it will implement key aspects of Pillar Two of the OECD/G20 Two-Pillar Solution to address the tax challenges arising from digitalisation of the economy.

Specifically, the announcement included the intention to implement the Global Anti-Base Erosion Model Rules (GloBE Rules). They provide for a coordinated system of taxation intended to ensure in-scope **multinational enterprise (MNE) groups** are subject to a global minimum tax rate of 15% in each jurisdiction where they operate.

This measure is now law. The legislation includes a:

- 15% global minimum tax for MNE groups with the
  - Income Inclusion Rule (IIR) applying to fiscal years starting on or after 1 January 2024, and
  - Undertaxed Profits Rule (UTPR) applying to fiscal years starting on or after 1 January 2025.
- 15% domestic minimum tax for MNE groups applying to fiscal years starting on or after 1 January 2024.

See **Global and domestic minimum tax** for more information on the implementation of Pillar Two of the OECD/G20 Two-Pillar Solution in Australia.

Strengthening the foreign resident capital gains tax regime

As part of the Budget 2024–25, the Australian Government announced it will strengthen the integrity of the foreign resident capital gains tax (CGT) regime to ensure foreign residents pay their fair share of tax in Australia and to provide greater certainty about the operation of the rules.

As such, proposed amendments will be made to non-resident CGT provisions in **Division 855** (Div 855) of the *Income Tax Assessment Act 1997*. The changes will apply to CGT events starting on or after 1 July 2025, and will:

- clarify and broaden the types of assets on which foreign residents are subject to CGT
- amend the point-in-time principal asset test to a 365-day testing period
- require foreign residents disposing of shares and other membership interests exceeding $20 million in value to notify the ATO, prior to the transaction being executed.

This measure will ensure that Australia can tax foreign residents on direct and indirect sales of assets, with a close economic connection to Australian land, more in line with the tax treatment that already applies to Australian residents. The new ATO notification process will improve oversight and compliance with the foreign resident CGT withholding rules, where a vendor self-assesses that the asset they have sold isn't taxable real property.

These reforms will also improve certainty for foreign investors by aligning Australia's tax law for foreign resident capital gains more closely with OECD standards and international best practice.

This measure is not yet law.

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Our commitment to you

We are committed to providing you with accurate, consistent and clear information to help you understand your rights and entitlements and meet your obligations.

If you follow our information and it turns out to be incorrect, or it is misleading and you make a mistake as a result, we will take that into account when determining what action, if any, we should take.

Some of the information on this website applies to a specific financial year. This is clearly marked. Make sure you have the information for the right year before making decisions based on that information.

If you feel that our information does not fully cover your circumstances, or you are unsure how it applies to you, contact us or seek professional advice.