TD 2002/20 - Income tax: if an Australian film production company alters its method of charging for film production services supplied to a foreign associate to account for the impact of the tax offset scheme under Division 376 of the Income Tax Assessment Act 1997, will the Commissioner apply Division 13 of Part III of the Income Tax Assessment Act 1936 or the Associated Enterprises article of a relevant double tax agreement to increase the charge?

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Taxation Determination

Income tax: if an Australian film production company alters its method of charging for film production services supplied to a foreign associate to account for the impact of the tax offset scheme under Division 376 of the *Income Tax Assessment Act 1997*, will the Commissioner apply Division 13 of Part III of the *Income Tax Assessment Act 1936* or the Associated Enterprises article of a relevant double tax agreement to increase the charge?

Preamble

The number, subject heading, date of effect and paragraphs 1 to 7 of this Taxation Determination are a 'public ruling' for the purposes of Part IVAAA of the ***Taxation Administration Act 1953*** *and are legally binding on the Commissioner. The remainder of the Determination is administratively binding on the Commissioner. Taxation Rulings TR 92/1 and TR 97/16 together explain how a Determination is legally or administratively binding.*
*[****Note:*** *This is a consolidated version of this document. Refer to the Tax Office Legal Database (http://law.ato.gov.au) to check its currency and to view the details of all changes.]*

Date of effect

This Determination applies to years commencing both before and after its date of issue. However, this Determination does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of the Determination (see paragraphs 21 and 22 of Taxation Ruling TR 92/20). Note: the previous Division 376 of the ***Income Tax Assessment Act 1997*** *was repealed and a new Division 376 substituted as part of the* ***Tax Laws Amendment (2007 Measures No. 5) Act 2007****. The legislative change is of no consequence to the continuing operation of this Determination.*

1. No, unless there is evidence that the arrangement would reasonably be expected to have a different pricing impact on a charge between independent parties dealing at arm's length in comparable circumstances.

2. Division 376 of the *Income Tax Assessment Act 1997* establishes a scheme that is intended to assist the competitiveness of the Australian film production industry by providing tax offsets for qualifying film production expenditure of Australian taxpayers.

3. An Australian film production company may be providing film production services under an agreement with a foreign parent or other associate. Australia's transfer pricing rules in Division 13 of Part III of the *Income Tax Assessment Act 1936* and the Associated Enterprises article of a relevant double tax agreement permit the Commissioner to adjust the amount the Australian film production company charges for its services to the amount

that would be charged between independent parties dealing at arm's length with each other in comparable circumstances.

4. In performing the comparability analysis required to apply an appropriate arm's length pricing method in such a case, the tax offset scheme should be taken into account. The tax offset scheme should be treated as a condition of the market for film production services in Australia, and taken into account in evaluating a taxpayer's transfer price in that market. This is consistent with paragraph 2.104 of Taxation Ruling TR 97/20, which accords with paragraph 1.55 of the OECD's 1995 *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations*.

5. The tax offset scheme might potentially have a number of differing market impacts, including:

(a) a company might enter the market and supply the relevant services for a given price where it otherwise would not;

(b) existing providers might supply the same services as before at a cheaper price; or

(c) existing providers might supply the same services as before at the same price (i.e., retain any tax offset benefits).

6. The impact in a particular case will depend upon the facts and circumstances, having regard to the reasonably expected impact on a charge between independent parties dealing at arm's length in comparable circumstances.

7. Given a competitive market for film production services in Australia, and the tax offset being widely available within the industry, a relative reduction in the Australian market price for such services is arguably a reasonably expected impact of the tax offset scheme on that price. On this view, the tax offset scheme improves the competitiveness of the Australian producer and enables it to earn 'normal' profits, rather than higher profits by retaining the benefit of an effective reduction in production costs. Accordingly, absent evidence indicating a different pricing impact in the particular facts and circumstances, the Commissioner will accept that the tax offset scheme may produce a relatively reduced transfer price for production services, and will not seek to apply the transfer pricing rules to the amount of the reduction. This is subject to the need for the taxpayer's profit outcomes to make business sense, and for its pricing decisions regarding the impact of the tax offset scheme to accord with what an independent party would do to protect its own economic interest (see paragraphs 2.6, 2.10 and 2.15-2.16 of Taxation Ruling TR 97/20).

Commissioner of Taxation
28 August 2002

Previous draft:
Previously released in draft form as TD 2002/D7.

Related Rulings/Determinations:
TR 92/1; TR 92/20; TR 97/16; TR 97/20

Subject references:

- arm's length dealings
- associated enterprises article
- film incentives
- film production services
- government industry subsidy
- transfer pricing

Legislative references:

- ITAA 1936 Div 13 of Pt III
- ITAA 1997 Div 376
- Tax Laws Amendment (2007 Measures No. 5) Act 2007

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