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FIRB TAX CONDITIONS IN M&A DEALS – THE CURRENT STATE OF PLAY

19 April 2016 | Australia, Brisbane, Melbourne, Perth, Sydney
Legal Briefings – By **Andrew Hirst**, **Toby Eggleston** and **Cameron Blackwood**

On 22 February 2016, the Treasurer announced the introduction of new 'tax conditions' as part of the FIRB approval process.

- The tax conditions are wide and create considerable uncertainty for taxpayers.
- In this article, we explore the current state of play including the draft Guidance Note that has been issued by FIRB.

On 22 February 2016, the Treasurer announced the introduction of new 'tax conditions' which apply to the FIRB approval process in connection with M&A deals.

Although the underlying policy of the conditions is entirely reasonable (i.e. to ensure compliance with Australian tax laws) the conditions have been drafted in an extremely broad manner and are creating considerable uncertainty for taxpayers and market participants. The standard conditions can be split into 5 categories, being:

- ongoing compliance with Australia's tax laws,
- requirements to provide information to the ATO,
- requirements to notify transactions to the ATO if there is a risk of either the transfer pricing provisions or the anti-avoidance provisions in Part IVA potentially applying,

- an undertaking to pay outstanding tax debts, and
- a requirement to provide an annual report to FIRB in relation to compliance with the conditions.

In situations where FIRB/the ATO consider that the transaction involves a particular tax risk, a further 2 conditions may be imposed – these may require the applicant to obtain a tax ruling, enter into an advance pricing agreement or provide ongoing tax forecasts to the ATO.

In our experience on deals since the announcement, FIRB are imposing the standard conditions on all applicants.

SPECIFIC CONCERNS ABOUT FIRB'S TAX CONDITIONS

Although, it is beyond the scope of this article to articulate all the concerns with the new tax conditions, we have set out a few below:

- there is no materiality threshold on the obligation to comply with tax laws – as such, a minor breach of the tax laws (for instance, lodging a return late) would appear to give rise to a breach of the conditions,
- many of the conditions impose obligations in relation to 'associates' of the applicant. Associates are defined very widely for tax purposes and extend well beyond members of the same group (for instance, to partners in a partnership). Although the obligations to ensure compliance by 'associates' is only to use 'best endeavours', this has the potential to cause significant practical and evidentiary difficulties,
- the information requirements are extremely broad requiring the provision of any information requested by the ATO in relation to the relevant transactions, operations or assets. Indeed, the provision is so broad that it appears to go beyond the detailed information request provisions that are contained in the Tax Acts. This cannot be correct – the ATO should not have wider information gathering powers under these conditions than Parliament has considered appropriate under the Tax Act,
- the conditions require an applicant to notify the ATO whenever the transfer pricing provisions or Part IVA 'may potentially apply' to the transactions, operations or assets. Again, the threshold for this test has been drafted at a very low level – it would have been preferable if the conditions had adopted a test that is recognised for tax purposes, such as a 'reasonably arguable position',
- the conditions require an applicant to have paid 'any outstanding tax debt' (or to use

best endeavours to ensure that an 'associate' has paid any outstanding tax debt). Although not directly stated this condition appears to be aimed at ensuring that the ATO has collected any previously outstanding tax debts – for instance, from a previous investment into Australia. The precise scope of this condition is again unclear if for example an existing tax debt is subject to dispute, and

- if there are joint applicants then the question of joint and several liability arises. At the moment, there does not appear to be anything preventing one applicant from being in breach if its co-applicant has breached one of the conditions. This is a fundamental issue which needs to be addressed.

COMMENTARY

We have been liaising with FIRB at various levels in relation to the tax conditions.

When these have arisen in the context of actual transactions we have being attempting to engage with FIRB to limit the scope of some of the conditions. For example, to ensure that the ATO's information gathering rights are limited to rights that currently exist under the Tax Acts. At this stage, we do not know whether FIRB and the Treasurer will accept any modifications to the conditions.

FIRB has issued a draft Guidance Note which attempts to provide further clarity in relation to the conditions. Although there are some helpful things within the draft Guidance Note (for instance, it confirms that parties are not required to provide any information which is subject to privilege), on the whole, the draft Guidance Note is of limited value – it provides little insight and does not address many of the issues that taxpayers are concerned about. We are currently working with industry bodies to provide a detailed submission on the conditions and the draft Guidance Note.

While the principles behind the conditions are reasonable in our view the drafting of the conditions is too broad. We hope that the consultation process may lead to changes – either in the conditions themselves or in the Guidance Note. If further clarity is not provided then there will be a real risk that, in the future, they will be administered in a way inconsistent with the scope of the original intention. This creates a significant risk when the ultimate consequence for non-compliance with the conditions is the potential divestment of the assets.

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.

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