Level 2
95 Pitt Street Sydney, NSW 2000
Telephone 02 8223 0000
Facsimile 02 8223 0077
Email tia@taxinstitute.com.au
Website www.taxinstitute.com.au
ABN 45 008 392 372

TAXATION INSTITUTE *of* AUSTRALIA
IT'S ESSENTIAL

11 September 2009

The Board of Taxation
c/- The Treasury
Langton Crescent
CANBERRA ACT 2600

Email: taxboard@treasury.gov.au

Dear Sirs,

Submissions re Review of the Application of GST to Cross-Border Transactions Discussion Paper July 2009

The Taxation Institute of Australia (**Taxation Institute**) welcomes the review by the Board of Taxation (**Board**) of the application of GST to cross-border transactions announced on 12 May 2009 and subsequently accompanied by the release of the Board's Issues Paper, *Review of the Application of GST to Cross-Border Transactions* (**Issues Paper**).

This submission addresses each of the questions in the Issues Paper, namely, those questions in chapters 4, 5 and 6 (also summarised in Appendix B) and, for ease of reference, adopts the same numbering. In addition to this submission, the Taxation Institute refers to the Taxation Institute's earlier submission in relation to the *Review of the Legal Framework for the Administration of the Goods and Services Tax* in respect of "International Issues" and an extract of those submissions is enclosed for the Board's reference in respect of this review.

The Taxation Institute notes, in particular, that the Board has not considered the GST-free exported services provisions, including, s.38-190(3) and refers to the Taxation Institute's earlier submissions in that regard. The Taxation Institute also notes that the Board has not considered the issue of taxable importations and creditable importations (see earlier submission) and suggests that a review of cross-border transactions should involve the examination of Divisions 13, 15, and related Divisions (for example,114 and 115) and, in addition, relevant interactions with the connected with Australia rules. For example, an additional issue raised is the uncertainty for non-residents regarding the sale of goods outside Australia which are then installed in Australia (s. 9-25(3)) and whether these supplies render the sale of goods subject to double taxation in Australia because of the later installation of the goods.

Unless otherwise indicated, all legislative references are to the *A New Tax System (Goods and Services Tax) Act* 1999 (**GST Act**) and *A New Tax System (Goods and Services Tax) Regulations* 1999 (**GST Regulations**).

4.1 What has inhibited the take up of voluntary reverse charge agreements?

There are numerous factors that have inhibited the take up of reverse charge agreements. These include:

(a) Accounting issues – it is often difficult for the recipient to capture reverse charge liabilities within their accounting system in an automated and systematic manner. Accordingly, the capture of

reverse charge liabilities often requires the recipient to adopt manual processes which is undesirable from an administrative, compliance and audit perspective.

(b) Lack of awareness – non-resident suppliers are often unaware of their obligations and options under the GST Act. This lack of knowledge may apply at a number of levels including:

a. The non-resident may be unaware that the supply of its services are otherwise taxable in Australia. This will often result in the supplier doing nothing in respect of GST unless compliance activities are commenced by the ATO (in the Taxation Institute's experience, the ATO has not actively audited international transactions). Hence, in many cases the non-resident supplier does not account for GST and accordingly does not consider the option of entering into a reverse charge agreement;

b. The non-resident is aware of its liability to account for GST, but is unaware that there is an option available to it of agreeing with its customer to enter into a reverse charge agreement. As a reverse charge agreement places an additional administrative burden on the recipient, the recipient may not inform the supplier that this option is available;

c. The non-resident (or its adviser) is unable to give a warranty that it does not make the supplies through an enterprise that "carries on an enterprise in Australia". Reverse charge agreements may only be used where the supplier does not make the supply through an enterprise that the supplier carries on in Australia, accordingly, it is necessary for the parties to determine this is the case before entering into a reverse charge agreement; and

d. The question of whether the non-resident carries on an enterprise in Australia is broader and different to the question of whether they have a permanent establishment for income tax purposes. Accordingly, the non-resident is not able to readily determine whether it is carrying on an enterprise in Australia or not.

(c) Reverse charge agreements cannot be entered into retrospectively – due to the lack of awareness by non-residents of their GST obligations, often the parties to a transaction are unaware of the potential GST liabilities until after they arise and the transaction has occurred. Currently the Commissioner does not allow non-resident suppliers and recipients to enter in a reverse charge agreements retrospectively.

(d) Requirements that the non-resident not be carrying on an enterprise in Australia – Division 83 only allows parties to enter into a reverse charge agreement where the non-resident does not make the supply through an enterprise carried on in Australia. Often the recipient will require a warranty to this effect prior to agreeing to enter into a reverse charge agreement. Further, because of the broad definition of "enterprise carried on in Australia" the non-resident will be unable to satisfy the requirement notwithstanding that they do not have a permanent establishment in Australia.

The suggested solution is:

(a) The Commissioner should issue further fact sheets advising non-residents of their main GST obligations and the option of using a reverse charge agreement with the customer to account for GST liabilities; and

(b) Division 83 should be amended to remove the requirement that the non-resident not make the supply through an enterprise it carries on in Australia.

4.2 Are the non-resident agency provisions unnecessarily limited?

The Taxation Institute assumes the reference to non-resident agency provisions is a reference to both Divisions 57 and 83 of the GST Act.

The Taxation Institute agree that the agency provisions in Division 57 are unnecessarily limited, in that they only apply to common law agents because a resident agent is liable for GST wherever a non-resident makes a supply "through" it. The operation of Division 57 is not dependent upon the resident

agent making an election to act as a resident agent, nor is it dependent upon the resident agent agreeing with the non-resident to act as a resident agent.

The expansion of Division 57 to other classes of "agency" would reduce the GST obligations of a large number of non-residents. However, unless the operation of Division 57 is made optional or voluntary, the expansion of Division 57 could expose residents to tax liabilities and obligations which they would not voluntarily assume. Australian resident entities may choose to alter their affairs so as not to be classed as agents, in these circumstances.

Accordingly, if Division 57 is expanded to include other classes of "agency" the application of the provision would need to be made voluntary and require an opt-in agreement.

In terms of Division 83, the requirement that the non-resident not make the supply through an enterprise carried on in Australia (refer s. 83(1)(b) and s. 83((2)(b)) is onerous and unnecessary. Removing this requirement would broaden the class of non-residents who could use reverse charge agreements and eliminate uncertainty as to whether specific non-residents are entitled to apply Division 83.

4.3 Do the non-resident agency provisions impose too much direct liability on the resident Australian agent? If so, how could the non-resident principal pay the correct amount of GST?

In its current form Division 57 imposes too much liability on the resident agent, without providing the resident agent with any and / or sufficient safeguards against the non-resident.

Division 57 imposes the entire liability on the resident agent for supplies and importations made "through" it by the non-resident. The provisions do not, of themselves, create an entitlement to seek any indemnity for any resulting GST liability from the non-resident. Unlike the Commissioner and / or the non-resident, the resident agent is unable to offset any GST liability / net amount against other input tax credits payable to the non-resident, except to the extent the non-resident makes an acquisition through or from that resident agent. Similarly the resident agent's GST liability may arise by reason of events outside the resident agent's control and / or knowledge (for example, the non-resident may not be registered for GST). A resident agent may not account for GST on supplies made by the non-resident through it on the basis that the non-resident does not exceed the registration threshold. The resident agent may be unaware of the fact that the non-resident makes other supplies causing it to be required to be registered.

Division 57 should be amended to only impose a direct liability upon a resident agent where the resident agent agrees to act as a resident agent. Further, Division 57 should be amended to give the resident a statutory right of indemnity against the non-resident for any GST amount paid on behalf of the non-resident (similar to s. 255(1)(d) of the *Income Tax Assessment Act 1936*.

4.4 Is your business being adversely impacted by on-line supplies and low value transactions? If so, what changes would you suggest to the current approach?

As the Taxation Institute has a diverse membership base, it is not possible to comment on the impact of on-line supplies and low value transactions, as the impact will vary between members.

CHAPTER 4 - Other Comments re GST registration and Permanent Establishment (PE) status

One of the most significant issues concerning the registration of non-residents for GST purposes is the issue of whether GST registration impacts upon whether that non-resident has a PE in Australia. Non-residents are often unwilling to register for GST in Australia due to the concern (which is usually unfounded) that such registration may result in the non-resident having a PE in Australia. The issue is propounded because there is nothing published by the ATO which confirms that the mere act of registering for GST will not cause an entity to otherwise have a PE in Australia.

The concerns of non-residents as to the impact of GST registration on their PE status can result in:

a) The non-resident having to obtain advice as to the impact of GST registration on their PE status. This advice adds to the cost of the non-resident carrying on business in Australia, and is often obtained at the cost of the Australian recipient;

b) The non-resident refusing to register for GST and / or requiring an Australian resident business to indemnify them for their Australian tax position; and

c) Non-residents structuring their affairs to avert the need to register for GST. This can result in the transaction been structured in a manner which is less attractive (in a commercial sense).

This significant impediment to the registration of non-residents for GST could be easily removed or reduced by the Commissioner confirming in a public ruling (or similar product) that the mere act of registering for GST will not cause a non-resident entity to otherwise have a permanent establishment in Australia. This technical issue is not controversial.

Option 1: Limit the application of the connected with Australia provisions

5.1 Would this approach reduce the number of non-residents that are unnecessarily drawn into the GST system? Does it raise any unintended consequences?

The Taxation Institute agrees that the approach outlined in option 1 would, to some degree, reduce the number of non-residents in the system. However, the option would only have a significant impact on the number of non-residents in the system if, as set out in other options, there is a mechanism for non-residents to obtain input tax credits without registering for GST.

As option 1 only applies where the non-resident does not have a business presence in Australia, the option will require the Australian business customer to determine whether their non-resident suppliers have a business presence in Australia in order to determine whether they need to account for a reverse charge liability. This could impose significant compliance obligations on Australian businesses.

Another unintended consequence of option 1 is the accounting and administrative issues associated with accounting for reverse charge liabilities. Presently, many accounting systems are not capable of automatically accounting for reverse charge liabilities, requiring manual intervention. This could become a significant compliance issue if the number of reverse charge transactions is expanded. The compliance issue could be minimised if the Australian business is only required to account for the reverse charge liability where it results in a net amount payable (i.e. the business is not entitled to a full input tax credit for the reverse charge liability).

Option 2.1: Shifting the GST liability of non-residents to residents through compulsory reverse charge

5.2 Should the compulsory reverse charge only apply where the acquisition is not for a fully creditable purpose?

In the Taxation Institute's view, the compulsory reverse charges should only apply where an acquisition is not fully creditable, as is presently the case.

Expanding the compulsory reverse charge to other Australian businesses could impose a substantial compliance cost on those businesses.

The number of non-residents required to be registered for GST could be reduced significantly by other changes to the rules regarding registration turnover (Division 188), GST-free supplies of rights and services (Subdivision 38-190), expanding the classes of resident agents (Division 57) and introducing options for claiming input tax credits without the need for GST registration. These options are preferable, as they maintain the GST revenue base without imposing additional compliance costs on Australian businesses (as would be the case if the compulsory reverse charge was expanded to fully creditable acquisitions).

5.3 Should the compulsory reverse charge apply to all supplies or just services and intangibles?

It is not necessary to expand the reverse charge to all supplies. A reverse charge is not required in respect of goods, as GST will apply at the point of importing the goods into Australia. Similarly, a reverse charge should not apply in respect of real property, on the basis that if the real property is outside Australia, consumption of the supply also occurs outside Australia.

The Taxation Institute notes that Division 84 presently refers to supplies of "services and intangibles" whereas other sections of the GST Act use the generic term "things" to refer to services and intangibles. It is foreseeable that the words "services and intangibles" may be found to refer to a narrower class of supplies than "things". To avoid unintended consequences and promote consistency, Division 84 should be amended to refer to "things (other than real property and goods)" and should not be limited to "services and intangibles".

5.4 Should the compulsory reverse charge apply to both registered and non-registered Australian businesses or only to registered Australian businesses?

In the Taxation Institute's view Division 84 already applies to non-registered businesses as s. 84-5(2) of the GST Act includes within an entity's registration turnover the value of supplies to which a reverse charge would apply. Accordingly, if an entity has a turnover of greater than $75,000 (including the reverse charge turnover) it will be required to be registered for GST.

No change should be made to the existing provisions. The existing provisions ensure entities are required to be registered where they have a turnover that parliament has determined is sufficient to require registration.

Option 2.2: Transfer GST Liability to an Australian subsidiary

5.5 Under Option 2.2 should a non-resident with a subsidiary in Australia be treated the same as a resident Australian business for GST purposes?

The Taxation Institute strongly opposes any option which makes an Australian subsidiary liable for the GST obligations of a non-resident parent or related entity. The imposition of such liabilities could discourage non-residents from operating in Australia, give rise to significant adverse accounting issue and may result in the Australian subsidiary breaching debt covenants. It would also adversely impact other shareholders and creditors of the Australian subsidiary.

The option of allowing an Australian subsidiary to account for GST obligations of its parent is currently available under the GST grouping provisions. These provisions allow the Australian subsidiary to be appointed as the representative member of the GST group. The Taxation Institute notes a feature of GST grouping, is that members of the group become jointly and severally liable for the GST obligations of the members of the group.

Alternatively, option 2.2 could be accommodated under option 4, by allowing an Australian subsidiary to elect voluntarily to act as its parent's tax representative in Australia. Such an option would not give rise to the problems under option 2.2, as registration as a tax representative would be voluntary.

5.6 What business relationships between a subsidiary and its-non-resident parent could this option apply to most appropriately?

If option 2 is introduced, which the Taxation Institute opposes, it should be restricted to GST groups, as is presently allowed for in the GST Act.

If option 2 is expanded to other relationships, the option should be voluntary not compulsory.

5.7 Should this option apply to entities other than subsidiaries such as subcontractors, who assist in delivering the non-resident's supply to an Australian recipient?

Option 2 should not apply to subcontractors. To expand the option to subcontractors would substantially increase the risk for subcontractors performing work for non-residents in Australia. In the

event of a default by the non-resident of its GST obligations, the subcontractor may be in no better position than the Commissioner to recover that GST from the non-resident.

Presently, option 2 applies to subcontracting arrangements covered by Division 57.

If option 2 is to be introduced and made to apply to subcontractors, its operation should be voluntary (i.e. require the subcontractor to make an election).

5.8 What type of supplies could this option apply to?

The question of what supplies option 2 should apply to depend upon what type of entities the option applies to.

If option 2 is restricted to wholly owned subsidiaries of non-residents, the option should apply to all supplies made by the non-resident. If the option is limited to certain classes of supplies:

1. it may produce unnecessary compliance costs as it would require the recipient to determine what is being supplied in order to determine whether it needs to account for a reverse charge liability; and

2. the option will not eliminate the need to register for a significant portion of non-resident businesses, as they will still need to register for GST where they make supplies not subject to the reverse charge provisions.

If option 2 is applied to subcontractors, it should be limited to supplies made by the non-resident through that subcontractor, similar to the current operation of Division 57.

5.9 Would this option be simple for taxpayers to comply with?

Option 2 would be simpler for non-residents where the supplies made by the non-resident are covered by the reverse charge provisions. This is because the option will remove the need for the non-resident to account for GST on supplies it makes. Further, if accompanied by other measures proposed in relation to the claiming of input tax credits, it may remove the need for the non-resident to register for GST.

However, option 2 shifts the cost of compliance from the non-resident supplier to the Australian business recipient. Option 2 will be more complex for the recipient as:

1. The recipient will need to develop processes for the processing of the reverse charge liabilities. Many accounting systems do not presently cater for such transactions; and

2. The recipient will incur compliance costs in ascertaining whether the non-resident is carrying on an enterprise in Australia and the correct GST treatment of the supply (i.e. taxable, GST-free or input taxed).

Option 2.3: Expanding the non-resident agency provisions

5.10 Are commission agents or sub-contractors likely to take up this option? If not, why not?

The Taxation Institute notes the present non-resident agency provisions are not optional; they apply wherever a non-resident makes a supply “through” a resident (i.e. no election is required to engage the operation of the provisions).

It follows that if Division 57 is expanded to include commission agents and sub-contractors, such entities will have no choice but to take up the non-resident agency provisions as they will be compulsory.

However, as set out above, the Taxation Institute recommends that if the non-resident agency provisions are expanded to include commission agents and sub-contractors, the operation of Division 57 be made optional.

Assuming Division 57 is made optional, it is unlikely that many non-resident suppliers will utilise this option unless it is accompanied with additional amendments:

1. removing the need for the non-resident to register for GST. Currently under Division 57 it is still necessary for the non-resident to register for GST; and

2. allowing for the non-resident to claim input tax credits without having to register for GST. Division 57 only allows the resident agent to claim input tax credits for acquisitions the non-resident makes through the resident agent.

Option 2.4: Non-residents be allowed to have a tax representative

5.11 Should options 2.3 and 2.4 apply instead of other options that reduce the need for non-residents to be in our GST system or should these options be used to supplement those circumstances where other options are ineffective?

The expansion of the non-resident agency provisions will not resolve the registration and compliance issues regarding non-resident suppliers, as they only apply where the relevant supply or acquisition is made "through" a resident agent (in an expanded sense). They will provide a helpful option for some non-residents where the resident agent is prepared to accept responsibility for accounting for GST as a representative of the non-resident.

Further, the expansion of the non-resident provisions will only be effective if they can be used in connection with other options tabled in the issues paper (e.g. option 3).

Accordingly, if option 2.3 and 2.4 are introduced, they should be introduced as supplements to other options proposed in the discussion paper.

5.12 Should options 2.3 and 2.4 be compulsory rather than voluntary?

For the reasons discussed above, the non-resident agency provisions should be made voluntary, particularly if, as proposed under options 2.3 and 2.4, they are expanded to include additional classes of entities.

Option 3: Non-residents not required to be registered for GST could be allowed a direct refund of any GST

5.13 Should the GST law provide a direct refund mechanism? If so, under what circumstances?

The Taxation Institute supports the introduction of a direct refund mechanism. Such a mechanism would be appropriate where the non-resident:

- is carrying on an enterprise; and

- is not registered nor required to be registered for GST in Australia.

However, the success of a direct refund mechanism will depend largely on the obligations imposed upon the non-resident in order to make a claim under the mechanism. If the obligations imposed are similar to those presently imposed in respect of non-resident registration, the mechanism may provide minimal relief for non-residents.

Whilst the Taxation Institute acknowledges that verification will be an essential part of any direct refund mechanism, the verification requirements will need to be balanced against the risk to revenue of any direct refund and the quantum of that refund. For example, the verification requirements may be linked to the quantum of the refund.

A direct refund mechanism which has a similar verification processes to those which apply currently for GST registration by non-residents will not significantly reduce the administration costs of non-residents.

5.14 Is a direct refund system necessary if the number of non-residents in the GST system is reduced under the options in this chapter?

Whilst other options tabled in the issues paper will, in some circumstances, reduce the number of non-residents required to be registered, a direct refund system is still necessary. This is because a substantial portion of non-resident's registering for GST are doing so voluntarily so that they may claim input tax credits for GST incurred in Australia.

Some options tabled in the issues paper (i.e. options 1 and 2) will only be successful if a direct refund mechanism is introduced. Options aimed at reducing the need for non-residents to register will only be successful if the non-resident is able to recover input tax credits in some other way without the need to register for GST. For example, whilst expanding the operation of the reverse charge provisions may result in a non-resident not being required to be registered for GST, in the absence of a direct refund scheme the non-resident will be required to register for GST if it is to claim input tax credits for any GST incurred by it.

5.15 Should direct refund system be based on reciprocal agreements with other countries as the case in some European countries?

This review builds upon recommendations made by the Board in its earlier review of the legal framework for the Administration of the GST. The focus of that and this review is streamlining and improving the operation of the GST, reducing compliance costs, and removing anomalies. The recommendations were to be broadly GST neutral.

Making any direct refund system contingent upon reciprocal agreements would be inconsistent with the Board's mandate. It will:

1. Increase compliance and administration costs of operating the direct refund system as it will become necessary for non-residents to demonstrate that a reciprocal arrangement applies in their home country; and

2. Result in embedded GST being passed onto Australian consumers and businesses. If non-residents are unable to claim input tax credits, these costs of the denied input tax credits are passed on to consumers in the form of increased prices.

Accordingly, any direct refund scheme should not be contingent on reciprocal agreements, unless, of course, Treasury were to obtain those reciprocal agreements from the overseas countries.

5.16 Should there be a more restrictive time limit for non-resident refund claims (as is the case in some foreign jurisdictions)? If so, how long should this period be?

The Taxation Institute can see no basis for a more restrictive time limit to apply to refunds lodged through a direct refund system. Again, such a recommendation would be inconsistent with the Board's mandate.

Further, the Taxation Institute notes that in practice the lodgement of a direct refund may take an extended time as:

1. any refund may need to be processed through a centralised accounts system located in an offshore head office; and

2. the imposition of Australian GST may not be initially apparent, meaning the entitlement of a refund to the GST may not be recognised until sometime after the acquisition is made.

For these reasons it would be inappropriate to shorten the period in which a direct refund is payable.

5.16.1 Should the direct refund scheme be restricted to certain supplies?

The Taxation Institute can see no basis for restricting the scheme to certain supplies. If the scheme is so restricted, it is likely to reduce the effectiveness of the scheme, as many suppliers will, at times,

make acquisitions outside the determined class, meaning they will be need to be registered for GST in any event.

Option 3.1: Supplies made to a non-resident but provided to a registered Australian business GST-free

5.17 Will the Australian supplier be able to readily identify situations where it provides a supply to a registered Australian business? In what circumstances might this prove difficult?

As the Issue Paper highlights at paragraph 5.58, in many situations the providee will be readily apparent. However, circumstances where it will be difficult to identify whether the supply is provided to a registered Australian business include:

1. Where there are numerous parties in the supply chain. For example, in Example 5 some of Audit Oz's services may be provided to Multi Co, and or both Multi Co and Oz Co.

2. Where the Australian supplier has limited interaction with the Australian providee. For example, IT Support P/L contracts with US Computer Co to provide IT telephone support to US Computer Co's worldwide customers. Customers may be based in Australia or outside Australia. Those customers in Australia may or may not be registered for GST. In this scenario, although IT Support P/L "provides" the support services it will not be readily apparent to US Computer Co who the customer is, where they are and whether they are registered for GST or not. Although IT Support P/L could ask the customer these questions, for commercial and privacy reasons, US Computer Co may not want the questions asked.

3. Where the services are amalgamated prior to the provision to the Australian recipient. In example 5, Audit Oz may provide limited audit services which are amalgamated to produce an overall audit report which is ultimately provided by Audit Intl to Oz Co. Services. In this scenario, although Audit Oz can identify who the Australian customer is, because the services where used to produce an amalgamated report, it will not be clear who it actually provided the services to (e.g. is it Audit Intl as it amalgamated the services into its report, or is it Oz Co Services because it receives the ultimate audit report?), which contains, amongst other things, what Audit Oz did.

4. Where the services are provided to an individual, in the course of the individual carrying on his / her enterprise or the enterprise of an Australian business (e.g. as an employee, partner, subcontractor or agent). In this scenario, the only way in which the Australian supplier will be able to identify whether the services were provided "for the benefit" of an Australian business is to ask the individual and rely on that representation.

5.18 Could this option be expanded to include supplies provided to employees or office holders of an Australian business or non-resident business? If so, how?

The non-resident provisions (e.g. s. 9-25 and s. 38-190) should be expanded generally to make it clear that where a service and or rights are provided to an employee or office holder (whilst acting as an employee or office holder), the service / rights are taken to be provided to the employer not the employee. This would remove the significant uncertainty which presently applies when identifying who the recipient of the service is.

Option 3.2: Supplies for consumption outside Australia

5.19 Do you consider that it is more appropriate that these supplies are taxable supplies with the registered recipient determining their entitlement to an input tax credit?

The Taxation Institute does not support amendments to make supplies taxable on the basis that the supply is made between two Australian GST registered entities but provided to an entity outside Australia. Such an approach would require the supplier to identify who they are contracting with as well as who the supply is made to, whereas presently the supplier is able to determine the tax status on where the supply is provided.

Option 3.3: Reverse charge for private consumers

5.20 Should Australia consider imposing a reverse charge on supplies to private consumers if those supplies exceed a threshold? How could this be enforced?

As referred to above, the focus of the Board's review and recommendations is streamlining and improving the operation of the GST, reducing compliance costs, and removing anomalies. The Board should not consider options which are designed to increase the revenue base, particularly where such options increase the overall complexity of the GST law.

Accordingly, the Taxation Institute do not support any option which imposes a reverse charge on private consumers if those supplies exceed a threshold.

Issues with imposing a reverse charge on private consumers include:

1. It is not always apparent that consumers are dealing with non-residents and or that the transaction is not subject to GST. Currently, when dealing with private consumers, businesses are required to use GST-inclusive pricing. In using a GST-inclusive price, it is not necessary to make clear whether that price includes GST or not. Further, businesses are not required to provide a tax invoice unless requested to do so by the customer. Accordingly, unless changes were made to require businesses to make it clear whether their prices include GST or not, it would not always be apparent to consumers whether they are purchasing services to which a reverse charge may apply.

2. There is likely to be wide-spread non-compliance because it will be difficult to identify transactions subject to reverse charge liabilities.

3. The approach would require private consumers to account for GST in respect of a tax which is designed to be accounted for business entities with suppliers as tax collectors, not consumers.

Option 3.4 – Changing the connection rules and GST liability transferred to an Australian subsidiary

5.21 Should option 3.4 apply to goods, services and intangibles?

The Taxation Institute notes that in example 7 under the present GST Act, Aussie Pics USA may be making a supply connected with Australia if:

1. 'the thing is done in Australia'. Although the meaning of this provision has not been considered judicially, according to the ATO and in the context of intangibles (such as the right to use a picture), the "thing" is done in Australia if the contract for the sale of the intangible is entered into in Australia;

2. Aussie Pics USA is making the supply through an enterprise it carries on in Australia. This may be the case where Aussie Pics USA makes the supply through a website with an Australian Internet Service Provider (ISP) (see TD 2005/2).

Accordingly, the mischief underlying option 3.4 could be addressed, at least in part, by the proper enforcement by the ATO of existing provisions. Further, the ATO could reconsider (or, at least, test) a broader interpretation of the term "thing is done in Australia", which includes the supply of intangibles where the benefit of that supply is enjoyed in Australia (i.e. adopting an interpretation which focuses upon the consumption of the supply as opposed to the contract granting the supply). In this regard, it is noted that the safe harbour provided by the ATO in GSTR 2000/31 about the thing being done being referable to the making of the contract, seems somewhat arbitrary, especially where contracts can be so easily made outside Australia, but the GST is a tax on a private final consumption in Australia.

If option 3.4 is adopted, it should only apply to services and intangibles. It is not necessary for the option to apply to the supply of goods, as imposition of GST on goods is addressed by the importation provisions.

5.22 Should the option be restricted to on-line supplies or apply more broadly?

If option 3.4 is introduced it should apply to supplies made through all sales avenues. To make the tax dependent on the different kinds of sales will result in compliance issues associated with determining whether the sale is or is not an on-line sale, and will create bias between suppliers dependent upon the sales avenue used by them.

Option 3.5: Review the low value threshold limit of $1,000

5.23 Is the importation threshold at an appropriate level? If not, what should this be?

A reduction in the threshold would result in a greater number of importations being taxed and accordingly, additional revenue. The taxation of additional revenue will increase administrative costs associated with collecting GST on importations.

The focus of the review should be on reducing administrative and compliance costs not increasing revenue. Accordingly, the Taxation Institute recommends against reducing the importation threshold at this time.

5.24 Should there be a connection between low value import threshold for GST purposes and for customs duty purposes?

The alignment of the low value import threshold for GST and the threshold for the application of customs duty reduces administrative compliance costs associated the identification of taxable importations, the collection of tax payable and importation of goods into Australia.

Accordingly, the Taxation Institute supports the alignment of the two thresholds.

Other options

The Board has not considered how the current operation of s. 38-190 impacts upon the complexity of cross border transactions, and specifically the need for non-residents to register for GST. The application of s. 38-190 needs to be considered by the Board.

As highlighted above, one of the main reasons a non-resident will be required to register for GST is to enable the non-resident to claim input tax credits. A common scenario where a non-resident is required to register is illustrated by examples 5 and 6. In these scenarios Audit Intl will register for GST in order to claim input tax credits.

The services supplied to Audit International would be GST-free under item 2 of s.38-190(1). However s. 38-190(3) deems the services not to be GST-free because they are “provided” to another entity in Australia. The purpose of s. 38-190(3) is to avoid consumers being able to avoid GST by subcontracting through a non-resident. This purpose could be achieved by limiting s. 38-190(3)(b) to supplies provided to another entity, which if acquired by that entity, are not acquired for a creditable purpose.

This option would have minimal impact on revenue, as in most circumstances the non-resident would be entitled to register for GST and claim an input tax credit (e.g. as occurred in example 5).

Under this option the supply from Audit International to Multi Co would also be GST-free under item 2 of s. 38-190(1). Accordingly, provided the GST-registration turnover is amended to exclude GST-free supplies, Audit International would not be required to be registered for GST in order to claim back the credits.

This option would:

1. Substantially reduce the complexity of cross-border supplies, as in most cases it would remove the need to consider whether the service is being provided to a non-resident (Audit Intl) or Australian resident (Oz Co. Services). The need to identify the providee in a cross–border transaction is one of the major issues that arises under s. 38-190(1); and

2. Remove the need for a significant portion of non-residents to register for GST. In example 5, Multi Co would still need to register for GST, but that is consistent with the GST framework, as Multi Co is making a taxable supply for consumption in Australia.

6.1 Would further streamlining of the registration process for non-residents still be necessary if the circumstances where non-residents need to register is significantly reduced because the options in Chapter 5 are implemented?

The options outlined in chapter 5 will not remove the need for all non-residents to register for GST and a substantial number of non-residents will still need to register.

Accordingly, irrespective of whether any of the options outlined in chapter 5 are introduced, it will still be necessary to consider the streamlining of registration procedures for non-residents.

6.2 Are there alternative ways of streamlining the registration process?

Other than the introduction of the options included in the Issue Paper, the Taxation Institute has not identified any alternatives to the streamlining of the registration process. However, the Taxation Institute considers that a review of s.38-190 of the GST Act may lead to less supplies being treated as taxable and consequently, fewer non-residents being required to be registered for GST. See the Taxation Institute's earlier submission (extracts attached).

In addition as submitted in the Taxation Institute's earlier submission (see extracts attached), the Taxation Institute considers that the registration and verification process needs to be aligned with the risk to revenue. For example, the verification requirements for a large multi-national with an Australian subsidiary should be different to a small business with no previous presence in Australia. Similarly the verification requirements should allow for a degree of discretion on the part of the Commissioner.

6.3 Options other than streamlining registration process for those non-residents that may need to stay in the GST system

For non-residents who are required to stay in the GST system the most appropriate method of administering their involvement is through GST registration (using a streamlined registration process).

The use of a direct refund system and or a tax representative should work as options in conjunction with and not as an alternative to streamlining the registration procedures.

6.4 Would any of the above introduce integrity risks, particularly those relating to revenue and identity fraud?

The introduction of a direct refund system, tax representatives and the streamlining of registration procedures will all involve integrity risks. However, the management of integrity risks needs to be balanced with the minimisation of administrative and compliance costs on non-residents.

6.5 and 6.7 What would be the most appropriate method of excluding these non-residents from being required to be registered for GST?

Non-residents who only make GST-free supplies could be excluded from the requirement to register by removing GST-free supplies from the definition of current GST turnover (s. 188-15(1)) and projected GST turnover (s. 188-20(1)). Alternatively, s. 188-15(3) and s. 188-20(3) could be amended to disregard any GST-free supply made by a non-resident. This measure could be limited to GST-free supplies made by a non-resident as opposed to GST-free supplies generally.

Another option not considered in the Issues Paper and which would reduce the number of non-residents required to register for GST is to amend the GST Act to remove s. 9-25(3)(b). That subsection provides that the supply of goods will be connected with Australia where the supplier installs or assembles the goods in Australia. Where the supplier is installing equipment with a value in excess of $75,000, s. 9-25(3)(a) results in the non-resident supplier being required to register for GST, notwithstanding the value of the services performed in Australia may be substantially less than the registration threshold. The importation of the goods will also be taxed as a taxable importation, resulting in two taxing points.

The removal of s. 9-25(3)(b) would not have a substantial impact on revenue as the importation of the goods would still be subject to GST. The service of installing the goods would also remain connected with Australia (under s. 9-25(5)) and subject to GST if the value of the service supplied by the non-resident exceeds the registration threshold.

6.6 Should the GST-free supplies made by a non-resident be included in the registration threshold but only to determine whether other supplies that are not GST-free should be subject to GST?

GST-free supplies should not be included in the GST threshold, even if it is only to determine whether other supplies that are not GST-free should be subject to GST. Such an approach, would in many cases reduce the effectiveness of option 4, as many non-residents will make incidental and or minor taxable supplier (well below the registration threshold) resulting in them being required to be registered for GST.

Option 5: Non-residents using an agent

6.8 What would be the best method of renewing the non-resident's requirement to register without undermining the taxable or creditable status of the supply or acquisition made by the non-resident?

The Taxation Institute's preferred option for excluding the requirement for non-residents to register under Division 57 is to deem supplies made by a non-resident principal to a third party through a resident agent to be a supply that is made by the agent to the third party, and not by the principal. A similar provision is contained in the agency provisions in subdivision 153B of the GST Act.

Under this option the requirement for the non-resident to register would be removed as the supply made by it would be taken to be made by the resident agent, not the non-resident principal and hence would not be included in the non-resident's registration turnover (or could be specifically excluded). The creditable status of any acquisition would not be impacted, as the resident agent would be taken to be making the supply.

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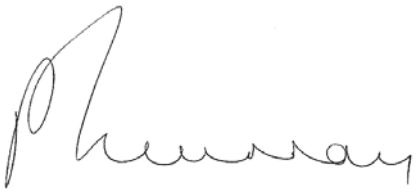
The Taxation Institute welcomes the opportunity to provide further clarification of any of the issues raised in this submission. Any queries concerning this submission should be directed to Taxation Institute's Senior Tax Counsel, Dr Michael Dirkis on (02) 8223 0011 or Jeremy Geale, Barrister, Victorian Bar on (03) 9640 3239 who, with contributions from other members, wrote this submission.

Yours sincerely,



Peter Murray