7 August 2015

General Manager
Corporate and International Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

Via Email: taxlawdesign@treasury.gov.au

Attention: Lucas Rutherford/Ronita Ram

Dear Lucas, Ronita,

Foreign Resident Withholding Regime

The Australian Financial Markets Association (AFMA) represents the interests of over 130 participants in Australia's wholesale banking and financial markets. Our members include Australian and foreign-owned banks, securities companies, treasury corporations, traders across a wide range of markets and industry service providers. Our members are the major providers of services to Australian businesses and retail investors who use the financial markets.

AFMA welcomes the opportunity to make a submission on the Exposure Draft and accompanying draft Explanatory Memorandum in relation to the proposed Foreign Resident CGT Withholding Regime. In making our submission, we have sought to focus on those matters that may affect the fair and efficient operation of the Australian financial markets and its participants.

Acknowledgement of previous submission

On 28 November 2014, AFMA lodged a submission in relation to the Treasury Discussion Paper titled "Non-final withholding tax on transactions involving taxable Australian property."

Our submission noted the concern with the withholding mechanism being with reference to assets considered to be "taxable Australian property" within the meaning of Section 855-15 of the *Income Tax Assessment Act* 1997 (**the 1997 Act**), and particular the consequences for foreign banks acting at or through a permanent establishment in Australia due to Item 3 of the table in that section. Accordingly, we are pleased with the legislative construction adopted in the Exposure Draft, namely to restrict the transactions

Australian Financial Markets Association
ABN 69 793 968 987
Level 3, Plaza Building, 95 Pitt Street GPO Box 3655 Sydney NSW 2001
Tel: +612 9776 7955 Fax: +61 2 9776 4488
Email: info@afma.com.au Web: www.afma.com.au

that give rise to a withholding obligation to transactions involving "taxable Australian real property" within the meaning of Section 855-20 of the 1997 Act. In addition, indirect real property interests, as determined with reference to Section 855-25 and Section 855-30 are included in the scope of transactions to which the proposed withholding applies.

Secondly, we noted in our submission that certain transactions will occur where there is no visibility between the buyer and seller, and indeed the tenet of anonymity is fundamental to the transaction. Accordingly, we are pleased with the proposed "on-market" exemption in Section 14-215(b), although we make comment below regarding the ambit of this exemption.

On-market transactions

Proposed Section 14-215(b) provides an exemption for a transaction which is "on an approved stock exchange, and the CGT asset is an interest listed for quotation in the official list of that exchange." While we welcome the exemption, we have issues with its precise language and believe that the ambit of the exemption may be refined.

Definition of "on an approved stock exchange"

Firstly, the list of "approved stock exchanges" in the *Income Tax Assessment Regulations* 1997 is often not contemporaneous and is indeed currently out of date. Schedule 5 notes the following exchanges, as they pertain to Australia:

- Asia Pacific Exchange Limited
- ASX Limited
- National Stock Exchange of Australia Limited
- SIM Venture Securities Exchange Limited.

The glaring omission is Chi-X, which became a holder of an Australian market licence in 2011 and is authorised to operate a financial market in Australia. Indeed, the *Corporations Regulations* has been updated to include Chi-X Australia Pty Ltd as an addition to the four prescribed exchanges set out above.

From a drafting perspective, and in order to ensure that there are no gaps between the time that an Australian financial market licence is issued and either the *Income Tax Regulations* or the *Corporations Regulations* are updated, we would advocate the on-market exemption being drafted with reference to a transaction effected on a financial market operated by the holder of an Australian market licence granted under Section 795B of the *Corporations Act*. This could be an addition to the "approved stock exchange" definition in the *Income Tax Assessment Regulations* 1997 to acknowledge the possibility of transactions being effected on financial markets outside Australia similarly being eligible for the exemption.

Acknowledgement of ASIC-registered crossing systems

Secondly, we submit that the "on-market" exemption be extended to include transactions effected on an ASIC-registered crossing system. An ASIC-registered crossing system, also known as a dark-pool, is a trading venue that, pursuant to the ASIC Regulatory Guide 223,

is an "automated service provided by a market participant to its clients that matches or executes client orders with orders of:

(a) The market participant;

(b) Other clients of the market participant; or

(c) Any other person whose orders access the automated service;

otherwise than on an order book of a licenced market."

In effect, this means that where the participant is a member of the crossing system, the participant may be able to match order from clients or other members without going through the "approved stock exchange"/holder of an Australian market licence. In doing so, the participant will need to adhere to the "best execution" principle for the client, meaning broadly that if the price available in the crossing system is better than that which could be obtained on a financial market, the participant will cause the transaction to be effected on the crossing system.

Any transactions conducted through a crossing system must be reported to a financial market on which the stock is able to be traded.

In such circumstances, the purchaser will still have no visibility as to the identity of the vendor, and indeed will not necessarily have any control as to whether the transaction is effected on the financial market or through the crossing system. Accordingly, the rationale for exempting transactions effected in the market applies similarly and should warrant the broadening of the exemption.

In AFMA's view, it is critical that obligations imposed by taxation legislation do not create an artificial distortion in relation to the same security merely because it is traded at a different market venue, and the economic result for the buyer and seller is the same regardless of the venue.

Restriction to transactions "on the official list"

Finally, we note that the proposed exemption is where the "CGT asset is an interest listed for quotation in the official list of that exchange." AFMA is aware of securities that are able to be traded on-exchange but are not included in the "official list" of that exchange. A key example is securities that are listed on the ASX under the "AQUA rules" and granted "trading status" under those rules but are not included in the "official list." There is no basis, from a policy perspective, for such securities to be excluded from the on-market exemption.

It is noted that the *Corporations Act* definition of "on-market" extends to transactions that are either defined as such in the rules governing the operation of the market or, in the absence of such rules, effected in the ordinary course of trading. This would appear to cover AQUA listed securities.

Extension to repurchase and securities lending arrangements

Repurchase agreements, reverse repurchase agreements and securities lending agreements are financing transactions undertaken by parties whereby a security (typically a listed share or debenture) is transferred from one party to another in exchange for

collateral (cash), which is capable of being used by the recipient of the security for the duration of the transaction. During the duration of the transaction, the entity that has either sold the security under a repurchase transaction or lent the security under a securities lending agreement will pay compensation for the use of the funds posted as collateral.

Such transactions may, in specified circumstances, give rise to a disposal of the security for tax purposes, depending on the structure of the transaction, the manner in which it is effected and the extent to which the transaction adheres to Section 26BC of the *Income Tax Assessment Act* 1936. Hence, from a capital gains tax perspective, these are transactions that may technically crystallise a withholding mechanism. However, from an economic and accounting perspective, such transactions are considered to be collateralised loans and the seller/lender would continue to recognise the security on its balance sheet.

The repurchase and securities lending markets in Australia are very large and represent a key source of funding and liquidity for Australia's institutions. Any requirement to withhold, or indeed ascertain the residence of the counterparty and/or seek a waiver, would significantly inhibit the efficient operation of the markets. Further, from a policy perspective, these are not transactions that expose the Australian revenue base to compliance risks.

AFMA would advocate a broad exemption for transactions that fall within the commercially accepted definitions of repurchase and securities lending transactions. There is a precedent for such a legislative construction; the recent amendments to the OBU provisions specifically includes "securities lending or repurchase arrangements" as eligible-OB activities and acknowledges (in the accompanying Explanatory Memorandum) that they should take their ordinary meaning. Further, we note the Assistant-Treasurer's media release from 29 June 2010 that, in the TOFA context, sought to clarify the taxation treatment of repurchase and securities lending transactions to align such treatment to the commercial substance of the transactions.

* * * * *

We appreciate the opportunity to provide a submission on the Exposure Draft. Please contact me with any queries.

Yours sincerely,

Rob Colquhoun
Director, Policy