

8<sup>th</sup> October 2021

Committee Secretariat  
Select Committee on Australia as a Technology and Financial Centre  
PO Box 6100  
Canberra ACT 2600

By email: [fintech\\_sen@aofc.gov.au](mailto:fintech_sen@aofc.gov.au)

Dear Sir/Madam

**Australia as a Financial & Technology Centre Advisory Group (AFTCAG)  
Submission on proposals for reform of Australia's Offshore Banking Unit regime**

The members of the Australia as a Financial & Technology Centre Advisory Group (AFTCAG) group are pleased to provide input in response to the Select Committee on Australia as a Technology and Financial Centre's examination of options to replace the Offshore Banking Unit (OBU) concessional tax regime.

We have set out in a high-level manner in the attached presentation:

- Our understanding of the issues raised by the OECD's Forum on Harmful Tax Practices which have resulted in the Australian Government repealing the OBU regime
- Proposed options to reform the OBU that would maintain and enhance Australia's global position.

We highlight that the OBU concessional tax rate could be aligned with the OECD's BEPS 2.0 project which is expected to include a Global Anti-Base Erosion Proposal minimum tax rate of at least 15% on a country-by-country basis (Pillar 2), which is intended to be met on a blended company tax rate basis. We note a blended Australian income tax rate for many taxpayers in the funds management sector would be a combination of a revised 15% OBU regime rate and their normal 25% tax rate for base rate entities (broadly companies with aggregated turnover less than \$50 million) in respect of other income, to achieve a blended rate in excess of the Pillar 2 minimum rate of 15%.

On this basis, the reforms would then only need to address issues with "ring fencing". Our alternative options are:

- Extending the OBU regime to similar Australian arrangements, with an Australian income cap = eligible foreign OB income (our preferred option)
- Extending OBU regime to similar Australian arrangements, with an Australian income cap = amount which eligible foreign OB income increases from date of effect.

Please do not hesitate to contact us to discuss the attached in further detail.

Yours sincerely

  
Andrew Low  
AFTCAG Chair  
On behalf of the Australia Finance & Technology Centre Advisory Group

**Australia as a Financial &  
Technology Centre Advisory  
Group (AFTCAG)**

**Proposals for reform of  
Australia's Offshore  
Banking Unit regime**

**October 2021**

# Background

# Background - OECD assessment and OBU removal

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The Australian OBU regime was listed by the OECD as a harmful tax practice in its OECD/G20 Base Erosion and Profit Shifting Project, Harmful Tax Practices - 2018 Progress Report on Preferential Regimes

- Australian government's 2018 announcement advised that the OECD concerns were:
  - The concessional tax rate
  - The ring-fenced nature of the regime

- Bill now enacted to reform OBU regime:
    - Removing concessional 10% tax treatment for OBU activities from 2023-24
    - Removing withholding tax exemption for OBUs for interest paid on or after 1 January 2024
    - Closing the regime to new entrants
- Government announced it would consult on alternative measures to provide industry support and ensure activity remains in Australia

## Background - Ring fencing from the domestic economy concerns

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- “Ring-fencing” refers to the concessions offered by the regime only being available to international and not domestic business
- These OB activities broadly include:
  - financial intermediation between offshore lenders and offshore borrowers
  - providing other financial services to offshore investors investing outside Australia
  - borrowing and lending activities; guarantee type activities; trading activities; eligible contract activities; investment activities; advisory activities; hedging activities; leasing activities; activities prescribed in the regulations
- Assessable income from eligible OB activities is effectively subject to a tax rate of 10 per cent rather than the corporate tax rate of 30%/25%, by bringing to account only an ‘eligible fraction’ of income from OB activities and associated expenses
- In addition interest payments made by OBUs when borrowing from offshore are not subject to interest withholding tax when the borrowed funds are used to carry on eligible OB activities

# Background - Impact of removal of OBU regime

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The purpose of the OBU regime is to encourage offshore financial transactions between non-residents to be conducted by an Australian institution, rather than by an offshore financial institution

The OBU regime targets what are highly mobile financial sector activities

## Removal of OBU impacts

- In a competitive environment between jurisdictions the removal of the OBU regime will result in the loss of this business by Australian providers with follow on loss of jobs and expertise
- Australian Treasury forecasts in the 2021 Federal Budget shows drop in receipts from the removal of the OBU regime of \$160 million in the period to 2024-25

# Proposals to address tax rate concerns

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- Is the OBU tax rate low?
  - OECD has not suggested what the minimum OBU tax rate should be for the regime not to fail this factor
  - Assumed focus is on the difference between the rate applicable to OB income and Australia's headline corporate tax rate (i.e. 10% v 30%)
  - Other aspects of the operation of Australia's tax system should also be taken into account when assessing if the OBU rate is unacceptably low
  - Rates should be considered against the competitive environment - 10% is higher than what would be the effective rate for such activities in other countries including Singapore and Hong Kong
- Replacement tax rate proposal
  - Rate could be aligned with the acceptable rate set under the OECD BEPS 2.0 project pillar 2 global minimum tax proposals
  - The 1 July 2021 agreement of Inclusive Framework jurisdictions on key components of Pillars One and Two proposed that the global minimum tax rate should be 15% or more, which is intended to be met on a blended company tax rate basis

## **Proposals to address ring fencing concerns**

# Proposals to address ring fencing concerns Alt 1 – matching Aus and foreign income

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OBU regime to be extended to similar types of Australian arrangements

- Income from Australian arrangements to only qualify to the extent of the eligible foreign OB income
- Qualification to be based on total income on a tax consolidated group basis and not by tracking arrangements

Application to Australian arrangements should be a choice reflecting potential new costs of compliance

- Current OBU participant OB income to be grandfathered
- Income from arrangements in place as at commencement date remain subject to revised OBU tax rate
- Intended to help ensure existing business is not moved offshore

# Proposals to address ring fencing concerns Alt 2 – incremental income approach

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OBU regime to be extended to similar types of Australian arrangements

- Income from Australian arrangements to only qualify to the extent that the eligible foreign income increases from the date of effect
- This limits eligible Australian income to a maximum of the new foreign eligible income
- Participants will therefore need to attract new foreign arrangements to obtain any domestic arrangement benefit
- Qualification to be based on total income on a tax consolidated group basis and not by tracking arrangements

Application to Australian arrangements should be a choice reflecting potential new costs of compliance

- Current OBU participant OB income to be grandfathered
  - Income from arrangements in place as at commencement date remain subject to revised OBU tax rate
  - Intended to help ensure existing business is not moved offshore

# Proposals impact

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### Impact of extension to Australian arrangements:

- Continuation of regime retains current activity
- Increase in rate from 10% to 15% helps offset inclusion of income from Australian domestic arrangements
- Limit of eligible income from Australian arrangements under either option limits any additional cost and should be revenue positive
- Requirement to maintain or increase foreign OB income results in tax on such income that otherwise would not be earned by Australian entities
- Maintaining and growing eligible OB income in Australia will lead to increased economic activity in Australia, including increased employment and promotion of Australia as a financial centre

# Matching proposal impact

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- Under current regime
  - OB income \$100 @ 10% = \$10
  - Aus income \$100 @ 30% = \$30
  - Total income \$200
  - Total tax \$40
- After proposal with no income growth
  - OB income \$100 @ 15% = \$15
  - Aus income \$100 @ 15% = \$15
  - Total income \$200
  - Total tax \$30
- After proposal with growth in income
  - OB income \$150 @ 15% = \$22.50
  - Aus income \$150 @ 15% = \$22.50
  - Total income \$300
  - Total tax \$45

Alternative scenario if no replacement implemented

- **All OB income moved offshore**
  - OB income \$0 @ 30% = \$0
  - Aus income \$100 @ 30% = \$30
  - Total income \$100
  - Total tax \$30

**Impact of no replacement regime vs after proposal with growth in income**

Lower economic activity in Australia

Loss of tax revenue from relocated business and reduced employment

# Incremental proposal impact

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- Under current regime
  - OB income \$100 @ 10% = \$10
  - Aus income \$100 @30% = \$30
  - Total income \$200
  - Total tax \$40
- After proposal with no income growth
  - OB income \$100 @ 15% = \$15
  - Aus income \$0 @15% = \$0
  - Aus income \$100 @30% = \$30
  - Total income \$200
  - Total tax \$45
- After proposal with growth in income
  - OB income \$150 @ 15% = \$22.50
  - Aus income \$50 @15% = \$7.50
  - Aus income \$100 @30% = \$30
  - Total income \$300
  - Total tax \$60

Alternative if no replacement - All OB income moved offshore

- OB income \$0 @ 30% = \$0
- Aus income \$100 @30% = \$30
- Total income \$100
- Total tax \$30

## **Impact of no replacement regime vs after proposal with growth in income**

Lower economic activity in Australia

Loss of tax revenue from relocated business and reduced employment