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**Financial Corporations (Transfer of Assets and
Liabilities) Amendment Bill 2002**

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I N F O R M A T I O N A N D R E S E A R C H S E R V I C E S

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No. 119 2001-02

Financial Corporations (Transfer of Assets and Liabilities)
Amendment Bill 2002

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Financial Corporations (Transfer of Assets and Liabilities) Amendment Bill 2002

Date Introduced: 12 March 2002

House: Senate

Portfolio: Treasury

Commencement: The legislation will be taken to have commenced on 1 July 2001

Purpose

To amend the *Financial Corporations (Transfer of Assets and Liabilities) Act 1993* (the Transfer Act) to allow more time for subsidiaries of foreign banks to convert to a branch structure and remain eligible for concessional tax treatment.

Background

The Transfer Act modifies the application of a number of the provisions of the *Income Tax Assessment Act 1936* (ITAA) as they apply to the transfer of assets and liabilities from locally incorporated subsidiaries of foreign banks to newly established branches of the parent foreign bank. The Transfer Act seeks to place the branch of the foreign bank in the same position as the subsidiary that has transferred the assets. In particular it modifies the ITAA to:

- defer the imposition of taxation in relation to the transfer of assets and liabilities until the asset or liability is subsequently disposed of by the receiving corporation
- make the capital gains roll over provisions applicable to the transfer of assets to which the Transfer Act applies
- allow the provisions relating to transfer of net capital losses to apply to transfers under the Transfer Act
- exempt the transfer of trading stock under the Transfer Act from tax
- allow for transfers of bad debts

Warning:

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- allow for exemption from interest withholding tax in certain circumstances, and
- allow for the transfer of losses.¹

Foreign Bank Branches

When the Hawke Government allowed the entry of foreign banks in 1985 it required them to be established as locally incorporated subsidiaries rather than as branches of the parent bank. In 1991, the House of Representatives Standing Committee on Finance and Public Administration recommended that subject to meeting certain matters, including prudential requirements, foreign banks should be allowed to operate in Australia as branches.² The prime benefit of such a move was said to be the possibility of increased competition in the banking industry. The Committee stated:

By having a broader capital base and improved fund raising capabilities, it is evident that a branch of a foreign bank would be in a far better position than a foreign bank subsidiary to compete against the incumbent domestic banks.³

In 1992 the previous Government decided to allow foreign banks to operate as wholesale banks in the form of a branch.

Following this decision, foreign banks had to determine whether they wanted to change the structure of their operations in Australia by converting subsidiaries to branches. The Transfer Act is intended to facilitate the reorganisation of business by bestowing concessional tax treatment on the transfer of assets and liabilities from a subsidiary to a foreign corporation that is an 'eligible foreign ADI' or the holding company of an eligible foreign ADI or a 'newly established local ADI'.⁴

An eligible foreign ADI is a foreign corporation that:

- has been authorised under the *Banking Act 1959* to conduct banking business in Australia, and
- received its authority before 22 December 1993 or obtained an authority pursuant to an application made before *1 July 2001*.⁵

A newly established ADI is a Australian company that was granted its banking authority:

- between the 18 June 1993 and the 22 December 1993, or
- obtained an authority pursuant to an application made before *1 July 2001*.⁶

Paragraph 7(6)(c) of the Transfer Act provides, *inter alia*, that the Act only applies in relation to the transfer of an asset or liability that occurs before *1 July 2004*.

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The Case for Amendment

As at February 2002, there were 12 foreign subsidiary banks operating in Australia.⁷ The Government introduced this Bill to extend the deadline for concessional tax treatment.⁸ It has stated that the extension is appropriate given that when the eligibility period expired on 1 July 2001 there was uncertainty in the industry about changes to the thin capitalisation rules and the consolidation regime which made it difficult for foreign banks to determine the appropriate structure of their operations.⁹

New thin capitalisation rules were introduced by the *New Business Tax System (Thin Capitalisation) Act 2001*. This legislation sets out the circumstances under which a deduction for interest payments which would otherwise be allowable will be reduced as an entity does not have sufficient equity compared to its debt levels. The rules apply to entities which operate both in Australia and overseas and are designed to prevent excessive claims relating to the Australian business of a multi-national operator. The legislation was introduced on 28 June 2001 and did not pass until 27 September.¹⁰

The consolidation regime will allow corporate groups to lodge a single tax return and be treated for taxation purposes as a single entity. While the Treasurer has stated that the consolidation regime will commence July 1 2002, no legislation to facilitate the change has yet been introduced to Parliament. It is likely that foreign banks will continue to be uncertain about their appropriate structure until the consolidation legislation is finalised.

Main Provisions

In order to extend the application of the concessional tax treatment **items 1 and 2** amend the definitions of 'eligible foreign ADI' and 'newly established local ADI' to include entities that are granted a banking authority pursuant to an application made before 1 July 2003.

Item 3 extends the deadline for any subsequent transfer of assets and liabilities from 30 June 2004 to 30 June 2006.

Endnotes

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- 1 Chris Field, Financial Corporations (Transfer of Assets and Liabilities (Amendment) Bill 1993, *Bills Digest*
 - 2 House of Representatives Standing Committee on Finance and Public Administration, *A Pocket Full of Change: Banking and Deregulation*, November 1991, Recommendation 10.46.
 - 3 *ibid.*, p. 159.
 - 4 Section 6 of *Financial Corporations (Transfer of Assets and Liabilities) Act 1993*.

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5 Section 3.

6 *ibid.*

7 There were 24 branches of foreign banks. A list of these banks is available on the APRA website: <http://www.apra.gov.au/ADI/ADIList.cfm#FSB>.

8 The Minister foreshadowed this legislation last August see: The Hon. Joe Hockey MP, 'Foreign Bank Tax Deadline Extended', *Press Release*, 22 August 2001.

9 Senator, the Hon. Ian Campbell, *Second Reading Speech*, Senate Hansard, 12 March 2002, p. 531.

10 More information on thin capitalisation can be found in *Bills Digest* No16 2001-2002.

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