



## MEDIA RELEASE

### AFMA Says Board of Taxation Should Call Time on LIBOR Cap

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AFMA's submission to the Board of Taxation's review of tax arrangements applying to permanent establishments has called for the Board to recommend the immediate abolition of the 'LIBOR cap'.

AFMA's Executive Director, David Lynch, said today:

"The LIBOR cap unnecessarily inhibits the flow of capital into Australia through foreign bank branches and, therefore, increases pressure on the availability and cost of credit to Australian business.

"The LIBOR cap is an archaic and punitive feature of the law that is inconsistent with internationally accepted transfer pricing principles. It makes Australia a harder place to do business for foreign banks who want to commit resources to Australia.

"The Board of Taxation should support the Johnson Report recommendation to abolish the LIBOR Cap. Removal of the cap is exactly the sort of measure that would fit within the Government's banking competition and growth strategy.

"By removing constraints to capital inflows, abolition of the LIBOR cap is expected to provide a modest net tax revenue gain for the Federal Government."

The LIBOR cap refers to Section 160ZZZA(1)(c) of the 1936 Income Tax Assessment Act, which caps the deductibility of interest paid by a foreign bank branch on funds borrowed from its overseas parent to LIBOR. That is, where funds are provided at a rate above LIBOR, the branch will be denied a tax deduction for those excess amounts.

The Australian Financial Centre Forum's report on *Australia as a Financial Centre* (the Johnson Report) stated in 2009 that the global financial crisis (GFC) highlighted the reasons why the LIBOR cap is a particularly inappropriate benchmark for the deductibility of interest. Its removal would contribute to more diversified funding sources and lower borrowing costs for consumers and business.

Abolition of the LIBOR cap would be unambiguously beneficial for banking competition in Australia. Some foreign bank branches have indicated that removal of the LIBOR cap would lead them to increase their lending activities in Australia and bring business into Australia that is currently conducted from overseas. Since the GFC, the market share of foreign bank branches, in terms of Australian resident assets, has fallen by over 40%.

AFMA has also asked the Board to recommend that Australia should be aligned with the OECD by adopting the functionally separate entity approach to determine the profits attributable to permanent establishments. The functionally separate entity approach should apply to domestic banks with offshore branch operations and the existing law for foreign banks with branch operations in Australia, which entrenches the functionally separate entity principle for most transactions, should be strengthened to apply to all financial transactions.

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**Notes for Editors:**

The Australian Financial Markets Association (AFMA) is the leading industry association promoting efficiency, integrity and professionalism in Australia's financial markets and provides leadership in advancing the interests of all market participants. These markets are an integral feature of the economy and perform the vital function of facilitating the efficient use of capital and management of risk. Market participants perform a range of important roles within these markets, including financial intermediation and market making.

AFMA represents over 130 members, including Australian and international banks, leading brokers, securities companies, state government treasury corporations, fund managers, traders in electricity and other specialised markets and industry service providers.