



A U S T R A L I A N C H A M B E R
O F C O M M E R C E A N D I N D U S T R Y

Taxation of Financial Arrangements

**ACCI Submission to
the Department of Treasury**

March 2007



1. BACKGROUND

The Australian Chamber of Commerce and Industry (ACCI) has been the peak council of Australian business associations for over 100 years.

ACCI is Australia's largest and most representative business association.

Through our membership, ACCI represents over 350,000 businesses nationwide, including:

- Australia's top 100 companies
- Over 55,000 medium sized enterprises employing 20 to 100 people
- Over 280,000 smaller enterprises employing less than 20 people

These businesses collectively employ over 4 million people.

ACCI's member organisations include the State and Territory Chambers of Commerce and Australia's leading national employer and industry associations. Our members represent all major sectors of Australian industry including small employers and sole traders as well as medium and larger businesses.

A list of ACCI members is attached.

2. BACKGROUND

The Government released an exposure draft of legislation relating to the Taxation of Financial Arrangements¹ in January 2007.

- Financial arrangements include debt, equity, derivatives, commodities and foreign exchange.

The Government argues that the current tax treatment of these arrangements is very ad hoc, complex and out of date, encouraging tax minimisation. The TOFA reforms are designed to make the law more systematic, reducing complexity and compliance costs while reducing tax minimisation.

In simple terms, the TOFA proposals mean that the gains and losses on most financial arrangements will be accrued rather than taxed on a realisation (cashflow) basis.

Some transactions are exempt from the accrual rules, including equity and trade credit. Most transactions of smaller business and individuals will be fully excluded.

Instead of using accruals, taxpayers can instead use other methods, including fair value (or market value), retranslation, hedging or financial accounts.

These alternatives are generally only available for taxpayers whose accounts are required to be audited under law.

This submission is in response to the exposure draft legislation.

1. Available from: <http://tofa.treasury.gov.au/content/default.asp>

3. ACCI RESPONSE

ACCI appreciates the development of the TOFA rules over time. The current draft is a significant improvement over the previous draft, particularly in relation to the definition of financial arrangement and in the character hedging rules.

However, ACCI has some remaining concerns over the current draft. These are outlined below.

3.1. Accrual rules

Under the TOFA accruals rules, taxpayers are required to assume that all economic variables retain their current value. The Government should explore some scope for using forecasts in the accrual rules.

The draft states that accrual only applies to “sufficiently certain” payments. This term needs further explanation and definition. This does not necessarily need to be in the legislation.

The draft requires taxpayers to re-estimate accrual amounts under a financial arrangements when circumstances arise that “materially affect the amount or value of financial benefits”. Technically, this means that accruals will have to be recalculated on a variable rate debt instrument (even an overdraft) every time the interest rate changes, which is unnecessarily complex. A simpler approach is needed for simpler arrangements.

3.2. Elective methods

Under the TOFA draft, the fair value, foreign exchange retranslation, and use of financial accounts elective methods are only available to taxpayers whose accounts are required to be audited under law. It is not clear why these elective methods should not be available to *all* taxpayers whose accounts are audited, even if this auditing is not required under law. There would be a number of businesses whose accounts are audited, even though this is not required by law.

3.2.1. Accounting

The rules relating to the accounting elective method should clarify the treatment of changes in accounting rules.

The conditions on the use of the accounting elective method appear excessive. The current rules require the total gain or loss on a financial arrangement to be the same under the tax and accounting method, and the difference in timing between the two has to “not be substantial”. The compliance costs with meeting this requirement for every transaction may be excessive.

It may be difficult to measure the difference between accounting and tax methods, when taxpayers have a choice of (other) tax methods. In particular, there may be significant differences between the accrual, fair value, hedging and retranslation methods, so it is not clear what the comparison should be with.

3.2.2. Hedging

There may be value in including a regulation making power in the table in Section 230-215 (which relates to character hedging). This would allow additional items to be added to the table more easily.

The table in Section 230-215 (which relates to character hedging) does not appear to include character matching for hedges relating to CFCs, FIFs and transferor trusts. There may be other character hedging items that are not included in the current draft. Either these items should be included in the laws or a regulation making power should be included to enable these items to be added later if and when concerns have been addressed.

3.3. Miscellaneous

It is not clear why the TOFA rules need special rules for whether losses are deductible, when these rules are already elsewhere in the law.

It is unclear why there need to be various different treatments of finance leases under TOFA and other current and proposed laws (including the proposed Division 250). The Government has been trying to reduce the length of the tax law, as well as limit any increases in the law. In this context, any scope for reducing duplicate new laws should be explored.

- However, we would not like to see any further significant delays in the proposed Division 250 to take account of this concern.

The Government should explore a *de minimis* exemption from TOFA for small-value transactions.

Detailed communication, particularly with medium size businesses, is needed when the TOFA proposals become law.

4. CONCLUSION

ACCI welcomes the development of the TOFA laws since the previous draft. However, we consider that a number of improvements still need to be made, particularly relating to companies that do not meet the small business exemption but are not large enough to be required to be audited. This could potentially cover tens of thousands of businesses.

5. ACCI MEMBERSHIP

ACT and Region Chamber of Commerce and Industry
Australian Business Ltd
Business SA
Chamber of Commerce and Industry Western Australia
Chamber of Commerce Northern Territory
Commerce Queensland
Employers' First TM
State Chamber of Commerce (New South Wales)
Tasmanian Chamber of Commerce and Industry
Victorian Employers' Chamber of Commerce and Industry
Agribusiness Employers' Federation
Air Conditioning and Mechanical Contractors' Association of Australia
Association of Consulting Engineers Australia
Australian Beverages Council
Australian Consumer and Specialty Products Association
Australian Entertainment Industry Association
Australian Hotels Association
Australian International Airlines Operations Group
Australian Made Campaign Limited
Australian Mines and Metals Association
Australian Paint Manufacturers' Federation
Australian Retailers Association
Insurance Council of Australia
Master Builders Australia
Master Plumbers and Mechanical Services Association Australia
National Electrical and Communications Association
National Retail Association Limited
NSW Farmers Industrial Association
Oil Industry Industrial Association
Pharmacy Guild of Australia
Plastics and Chemicals Industries Association
Printing Industries Association of Australia
Restaurant and Catering Australia
Standards Australia Limited
Victorian Automobile Chamber of Commerce