Australian Banking Association

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Principal Adviser
Corporate and International Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

Via email: corporatetax@treasury.gov.au

Dear Principal Adviser

The digital economy and Australia's corporate tax system

The Australian Banking Association (**ABA**) appreciates the opportunity to provide comments on Treasury's Discussion Paper: *The digital economy and Australia's corporate tax system October 2018* (**discussion paper**).

With the active participation of its members, the ABA provides analysis, advice and advocacy for the banking industry and contributes to the development of public policy on banking and other financial services. The ABA works with government, regulators and other stakeholders to improve public awareness and understanding of the industry's contribution to the economy and to ensure Australia's banking customers continue to benefit from a stable, competitive and accessible banking industry.

General Comments:

The ABA is of the view that the activities of banks in Australia are appropriately taxed in Australia and the offshore jurisdictions in which they operate. Banks in Australia contribute a significant quantum of total corporate taxes paid in Australia and do not structure their tax affairs through low taxing jurisdictions. They were, therefore, not the obvious target of the recent OECD Base Erosion and Profit Shifting (**BEPS**) actions. In addition, banks in Australia are highly regulated entities and do not, as an ordinary course of business, engage in providing digital services that are not already subject to tax.

If there is to be any substantive change to the taxation rules impacting digital business, the ABA is of the view that this should be done with consensus of the OECD member nations and as a result of due consideration and consultation between member states and their taxpayers. The OECD is due to release its final report in 2020 which will provide the Government with clarity around what reform, if any, is required. Until the OECD publishes its view, the ABA does not support any interim measure, including the introduction of a digital services tax. If unilateral action is pursued in Australia or any other country, this could result in taxpayers being subject to double taxation.

Other jurisdictions have considered introducing a digital services tax to target services such as digital advertising, online intermediation and transmission of data. Financial services do not fall within the scope of those services targeted by recent announcements in Europe.

We attach for your reference, two separate papers prepared by banking groups:

- International Banking Federation (**IBFed**) paper dated 25 September 2018
- European Banking Federation (**EBF**) letter to the EC dated 15 November 2018

The ABA welcomes the discussion paper and our response follows:

1) Is user participation appropriately recognised by the current international corporate tax system? If not, how should value created by users be quantified and how should it be taxed?

The ABA is of the view that the existing corporate tax framework adequately captures profits earned by banks. Banks utilise data that they obtain from their customers to provide services which in turn are subject to tax. Accordingly, to the extent that there is any monetisation of data by a bank, this will be reflected in the profits subject to taxation. Where data is mandated to be exchanged for no value between a bank and third party for no fee, for example under an Open Banking framework, this transaction should not be subject to tax. Where a value added service in respect to customer data is provided to a third party, the profit should be subject to tax under ordinary principles.

2) Is the value of intangible assets including 'marketing intangibles' appropriately recognised by the current international corporate tax system? If not, how should value associated with intangibles be quantified and how should it be taxed?

3) Are the current profit attribution rules 'fit for purpose'? If not, how should profits be attributed?

The OECD Report on the Attribution of Profits to Permanent Establishments (2010) is well accepted guidance for banks on the attribution of profit between their head office and offshore branch operation. The ABA is of the view that these rules function appropriately to provide for the correct arm's length allocation. Australian Taxation Office (**ATO**) guidance and industry practice is well understood and established on profit attribution principles. Accordingly, any deviation from those principles would cause significant impact to banks and their operations. For example, a lengthy consultation was required to determine the appropriate methodology for allocation of profits from global derivative trading activities by banks.

4) What are your views on allocating taxing rights over residual profits associated with: (i) user contribution to 'user' countries, or (ii) 'marketing intangibles' to market countries?

5) Should existing nexus rules for determining which countries have the right to tax foreign resident companies be changed? If so, how?

6) From a tax perspective, do you consider that the digitalised economy is distinguishable from traditional economy? If yes, are there economic features of the digitalised economy that present special challenges in the context of taxation? How are these features relevant for assessing the costs and benefits of various models of taxation?

7) Can and should any changes to the international nexus and profit attribution rules be ring-fenced to apply only to highly digitalised businesses? If so, how?

The ABA considers that changes to the international nexus and profit attribution rules should only be undertaken with international consensus, which may or may not apply on a ring-fenced basis to highly digitalised businesses. If any unilateral measures are adopted, these should be very specific, targeted and clear that they do not have application to banks.

8) Are there changes other than to nexus and profit attribution rules that should be made to the existing international corporate tax framework and/or Australia's tax mix to address the challenges presented by globalisation and digitalisation?

The ABA understands that there is growing consensus among some jurisdictions (e.g. Germany) in relation to the introduction of a global minimum tax. Whilst little detail is available, it is possible that such tax may operate as:

- Adoption of a minimum tax rate which no state can avoid applying (and no multinational can avoid paying); or

- A disallowance of tax deductions (or similar adjustment) within a jurisdiction where there is a mismatch in the equivalent minimum tax applicable in the other jurisdiction.

From the ABA's perspective, this has the potential to impact all multinationals (not only banks) which have operations in low tax jurisdictions. It would be important to identify the appropriate base and rate for a global minimum tax. The tax should apply to the existing base to avoid double taxation, and currently there is significant divergence between the corporate tax rates of many OECD member countries (such as the UK), and Australia. Banks in Australia should not be unfairly penalised because of the relatively high corporate tax rate in Australia relative to its major trading partners. Again, the Government should not seek to implement such measures without global consensus.

9) What does the experience of other countries that have introduced interim measures or that are contemplating them mean for Australia?

To the extent to which other countries implement interim measures that impact financial services, there is the potential for unintended tax consequences for banks in Australia. Accordingly, as outlined in our response for question 13 interim measures should be limited in scope to exclude financial services, and this exclusion should be comprehensive.

Banks make their commercial decisions with consideration of various factors, including operating costs / risks in other countries (such as capital, funding and taxation). In the absence of international consensus, to the extent to which banks in Australia are subject to any digital tax on the provision of their financial services, this may influence / impact the extent to which they provide services within a particular jurisdiction. Banks in Australia largely operate through branch structures in offshore jurisdictions, therefore any implementation of measures offshore could result in a disconnect between banks onshore and offshore operations (where financial services are not excluded).

10) Should Australia pursue interim options ahead of an OECD-led, consensus-based solution to address the impacts of the digitalisation of the economy on the international tax system?

No, Australia should not pursue interim options ahead of the OECD-led, consensus-based solution.

If unilateral action is pursued, this could result in taxpayers being subject to double taxation (where credits are not available). If the Australian Government ultimately decide to pursue an interim measure, in addition to an exclusion for financial services, the Government should not require banks to become a withholding agent. The cost and complexity of such a feature in any interim measure would result in unreasonable and significant regulatory costs being placed on banks which would not be commensurate with any benefit.

11) What indicators could be used to identify businesses that benefit most from user-created value? Would an interim measure applied to digital advertising and/or intermediation services accurately target that value? How broadly or narrowly should 'digital advertising' and 'intermediation services' be defined?

12) The choice of 'nexus' for an interim measure (or a longer-term 'virtual' PE proposal) involves significant trade-offs between ease of administration and the risk of avoidance. Which nexus option strikes the best balance between these considerations?

13) What are your views on thresholds for an interim measure, taking into account the need to meet Australia's international trade obligations?

The ABA does not support the implementation of an interim measure and is of the view that reform should be actioned with international consensus following the OECD's final report in 2020.

Should an interim measure be introduced such as a digital services tax, all financial services should be excluded from the scope of such measures. It is the expectation that all financial services and peripheral services provided by banks would be excluded including all traditional online and digital services provided to customers, and trading/execution platforms, clearing house and collateral services.

The accurate targeting of such measures is essential given that the rules are generally revenue based and could (based on revenue) apply to large multinational banks.

Based on the existing European Commission rules to date, it is unclear whether certain types of financial services will be excluded under the rules. Article 3(4) of the Directive[1] provides for an exemption from financial services, however certain services may not be included within the exemption. Some concern has been raised in relation to:

- Trading facilitation (pre and post), trading venues and execution platforms for financial market transactions – these may allow members to buy and sell financial products and securities, commodities or foreign exchange. The platforms may operate to provide an interface for matching of transactions between members.
- Portfolio compression – where counterparties to derivative transactions can net off their positions via a digital platform.
- Trading venues established in the EU facilitating the trading of non-MiFID[2] products or trading venues established outside the EU.
- Fees charged by non-EU trading venues to members in the EU.

The ABA broadly supports the view of the EBF, as noted in their submission (attached), a "clear exemption must be provided not only for ad hoc payments, trading venues or crowdfunding, but for all types of financial and banking services".

We note the that the UK has announced that it will exclude financial services, with the business activities specifically considered not in scope of a digital services tax to include "the provision of financial or payment services - these activities are not considered to derive significant value from user participation and are often subject to unique tax and regulatory regimes already. Financial and payment services will not therefore be in-scope of the DST". The ABA will await further guidance on the precise scope as to what will be included. Consultation on the measures closes on 28 February 2019 and details will become available thereafter.

Yours faithfully

Signed by

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[1] Council Directive COM (2018) 148
[2] Markets in Financial Instruments Directive