

INTERNATIONAL FINANCIAL CENTRE - POSSIBLE REPEAL OF U.S. WITHOLDING TAX.

In our comment on proposals to develop Australia as an international financial centre we warned that the possible abolition of U.S. withholding tax might reduce the size of the Eurobond market by taking away the disincentive for foreigners to acquire U.S. based bonds. As U.S. withholding tax is 30 per cent, its existence reduces the yield of foreign holders of U.S. bonds from about 12 per cent to 8.4 per cent : The Economist 3 March 1984 at 16. However the 30 per cent rate may be reduced by the relevant double tax agreement. For example Article 11(2) of the (1982) U.S. Australian Convention reduces the rate to 10 per cent. A favourite method for U.S. corporations to avoid U.S. withholding tax is to establish finance subsidiaries in the Netherlands Antilles. Foreign tax credits are then claimed against Antilles tax. Different bills have been introduced into Congress. One is to repeal the tax with some minor exceptions. Another is to reduce it to 3 per cent or to replace it with a tax in that amount on all interest payments to foreigners, even in the Euromarkets. The different proposals are discussed in detail in the January 1984 issue of Investment/USA Vol 6 No.1 at 5.

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INTERNATIONAL FINANCIAL CENTRE - PROPOSALS CONCERNING AUSTRALIAN WITHOLDING TAX AND THE EURO AUSTRALIAN DOLLAR MARKET.

The Whitlam Report on offshore banking (discussed separately in more detail in this issue) argues that the existing withholding tax of 10 per cent should also apply on loans booked through the proposed OBU's (Offshore Banking Units). However, the Report proposes a penalty rate of "say 20-30 per cent" on foreign currency loans to Australian residents booked offshore and not through an OBU. Because of the fact that Australian banks are not taxed on a global basis, there is an incentive to book such loans through offshore subsidiaries in jurisdictions where the tax rate is lower than our 46 per cent. The Whitlam Report did propose that corporate tax (i.e. the tax on profits from OBU's, a separate tax to the withholding tax on interest paid by Australians to foreigners) on OBU's "pure" offshore transactions be 10 per cent. "Pure" offshore transactions are those between non-residents and in foreign currencies. Further, the Committee considered the problem of the offshore Australian dollars, the Euro-Australian dollar market. In submissions to the Campbell Inquiry, it was admitted that it was difficult to gauge the size of this market. The Whitlam Report indicates various ways in which the Euro-Australian dollars could be brought home to the advantage of the new OBU's. First Australian banks could be taxed on a global basis. The principle of neutrality would suggest then that all Australian business be similarly taxed, which would not be well received by those who have expanded overseas. Second, profits on "pure" offshore Australian dollar

transactions - i.e. those between non-residents - booked through Australia - could be taxed at 10 per cent rather than 46 per cent. The Whitlam Report recognised a potential tax avoidance problem here if domestic transactions were to be disguised as "pure" offshore Australian dollar transactions. However it did not think the difficulties unsurmountable.

REFORM IN LONDON:

For generations the City of London has been entrenched in traditional practices which are being abandoned under Government pressure. Negotiated commissions, corporate membership, increased foreign investment and the likely disappearance of the division of the profession into brokers and jobbers are some of the changes anticipated. It is expected that this will result in a strengthening of the City and its continued survival as a major financial centre. "Where else do you get such good backup- in terms of lawyers and accountants - and at times it enables to you deal with Asia in the morning and the U.S. in the afternoon. It will remain one of the world's three great financial battlegrounds". According to Euromoney, February 1984 at 28, its shape may change out of recognition.

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LEASING:

In a series of articles in Euromoney, February 1984, at 106, the latest developments in this international industry are discussed. Reflecting on legislation stopping cross-border leasing one authority is quoted as saying "Tax authorities the world over seem to have gone to the same school. They see leasing as costing them revenue, whereas it is really only deferring revenue". In this regard, it will be recalled that Australia too recently removed the fiscal advantages for leasing, usually of aeroplanes, to non-residents at the same time as removing the advantages of leasing to tax exempt authorities so graphically illustrated in the Eraring leasing arrangement. The articles argue that there are distinct advantages to the economy in cross-border leasing. In a separate article on aircraft leasing, the example of the utility of leasing to a developing country is cited. Mozambique, with a Marxist Government, needed to finance the acquisition of an 8-year old D.C.10, valued at \$US21 million. It was bought from Air New Zealand, registered in France with a French bank as the official owners. Although it operated from Maputo the lease was subject to U.K. law and the U.S. dollar finance was provided by an American bank based in London.

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