onesteel

OneSteel Taxation
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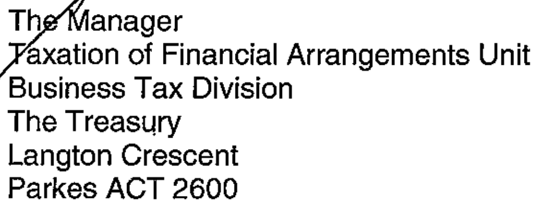

The Manager
Taxation of Financial Arrangements Unit
Business Tax Division
The Treasury
Langton Crescent
Parkes ACT 2600

Dear Sir,

Taxation of Financial Arrangements Stages 3 & 4 – Exposure Draft

Following on from the submissions made on the above exposure draft especially those made by Ernst and Young and the joint submission by CPA Australia and the CTA, OneSteel would like to raise its concerns on the exposure draft. As primarily a manufacturing and distributing organisation we feel that the legislation as proposed impacts on OneSteel adversely in ways not intended.

Principle based legislation:

Whilst we welcome the principles based approach to framing new legislation we believe that in this case the legislation does not meet the goals of principle-based legislation. In particular we feel that the structure of the legislation fails in the first instance to establish what a financing arrangement is and limit the legislation to just those arrangements. As discussed in the Ernst & Young submission the proposed section 230-10 is not clear and the legislation does not meet the stated purpose of aligning treatment with accounting or commercial treatments.

In our opinion, the proposed legislation does not define a financing arrangement in such a way that it will be more closely aligned with commercial recognition of gains and losses from financing arrangement as per its objective. Instead it seeks to make any legal or equitable "right to receive" or "obligation to provide" economic benefits in the future to be a financing arrangement. This all-encompassing academic definition is unbelievably wide and will capture many things that are not a financing arrangement by any commercial or accounting definitions. Some of these are identified as exclusions but again these definitions are at times arbitrary (eg a trade debtor who 364 days late is not a financing arrangement but is one the next day) or tied to tax definitions rather than aligning with accounting. A good example of failure of the definition to align with commercial reality is that personal services arrangements such as employment contracts have to be specifically excluded from the "definition".

Long term construction contracts and leases or contracts with a delayed final payment dependent on performance

The treatment of long-term construction (or some operating lease) contracts as financing arrangements may have unintended consequences for OneSteel and other manufacturers. It is not uncommon in our plant construction contracts (which are generally take shorter than 12 months to complete) to have a performance payment clause. For example, an item of plant may cost $1 million dollars to construct

over a 4-month period. It may have a payment schedule with an up-front payment and monthly progress payments. At the end of the construction and commissioning phase only 95% of the total contract value may have been paid. The remaining 5% would be payable after 12 months dependent on the plant meeting certain performance goals. As we would generally expect that what has been installed will achieve the goals then it could be argued that it is "reasonably likely" that these payment will be made. This payment is likely to be considered a financing arrangement extending over more than 12 months under this proposed legislation. Clearly it is not.

In general we see that the whole approach does not meet the objective of alignment with accounting gains and losses by:

- The failure to define a financing arrangement in a way that restricts it application to financing arrangements by generally accepted definitions, and
- The reluctance of the legislator to truly align with accounting standards especially under IFRS. Instead concepts similar to but not the same are adopted. By doing this the affected transactions will need to treated separately and differently from accounting practice. This is nothing new but the wide definition means it will occur more often.

On the whole the legislation as proposed will increase the need for a different tax treatment from both the current tax treatment and the accounting treatment. It will increase the level of interaction and documentation required for tax in such a way that it can be different from what is required for accounting. For example the treatment of hedges is different from hedges under IFRS and tax teams will need to work more closely with company treasuries to meet this legislation then they currently need to do.

This increase in complication is enhanced by the different treatments allowed depending on if you a small business or individual, a business audited under Chapter 2M or comparable foreign law and by the variety and precedence of elections. This is a clear example of inequity in the treatment of otherwise similar taxpayers or similar transactions and will increase the disparate distortional effects of different available taxation treatments.

I hope that this submission can be included in your deliberations given that you will receive it after the due date. If you wish to discuss this further please contact me as below or on 0407 291 107.

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