Australian Securitisation Forum

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Mr William Potts
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Dear William

Australian Securitisation Forum (ASF)[1] – Pillar 2 legislation and Australian securitisation vehicles

I refer to the discussion held on 18 July between members of the ASF's tax working group and you and your colleagues. On behalf of the ASF's tax working group, we set out below a summary of the key points from that discussion including a response to the additional question you posed in your email of 19 July:

ASF concerns for Treasury's consideration

1. As currently drafted, the Assessment Bill potentially results in a Domestic Minimum Top-up Tax allocation to securitisation vehicles, particularly for corporate vehicles.

[1] The ASF is the peak industry body representing the Australian securitisation and covered bonds markets. The goals of the ASF are to facilitate the formation of industry positions on policy and market matters, represent the Australian industry to local and global policymakers and regulators and to advance the professional standards of the securitisation industry.

2. Additionally, section 128-5 of the Consequential Bill would expose all securitisation vehicles, by virtue of being a Group Entity, to joint and several liability for any Pillar Two amounts payable by the MNE Group (with not even a requirement for default by the head company). We note that there is no Australian law preventing securitisation vehicles from entering into an arrangement under which it becomes subject to a tax liability, so section 128-5(2) does not assist.

3. As discussed, securitisation transactions generally require as a critical element that the securitisation vehicle be completely tax neutral, i.e. not exposed to the imposition of any tax, and not exposed to the tax debts of the sponsor group. This is because there are typically no excess funds in a securitisation structure from which to pay additional taxes, and the vehicle operates merely to repackage the income flows into a securitised form. These vehicles must be insolvency remote (i.e. not exposed to the credit risk of the sponsor), as it is this that allows access to cheaper funding than might otherwise be available, which in turn benefits ultimate borrowers.

4. We submit that this should be remedied by excluding securitisation vehicles from primary and secondary liability under the Assessment and Consequential Bills.

5. The appropriate definition to adopt for securitisation vehicles should be any entity that meets the conditions in section 820-39(3). Section 820-39 has effectively been the working definition for securitisation entities since it was introduced in 2003 by the *Taxation Laws Amendment Bill (No. 5) 2003*. We note that this was in response to excessive narrowness and rigidity in the definition of securitisation vehicle in section 820-942 – see for example paragraphs 1.6 and 1.14 of the Explanatory Memorandum to the Bill.

6. This would be consistent with the June 2024 edition of the OECD Agreed Administrative Guidance on the Model Rules (**OECD Guidance**), which contemplates that securitisation vehicles may be excluded from the DMT, without causing the DMT to be ineligible for QDMTT status.

7. We note that it would not be appropriate or effective to seek to create a new legislative definition of securitisation entity based on the OECD Guidance. This is because that definition has not been drafted with Australian law and practice in mind and would not capture typical Australian securitisation vehicles. In particular, that definition requires that the entity "pays out all cash received from its assets to its creditors… on an annual or more frequent basis", other than "cash retained… for eventual distribution to equity holders…", but the cash so retained must be *negligible relative to the revenues of the entity.* Australian securitisation structures, which widely employ a cash extraction mechanism based on distributions on equity, would likely fall outside this definition.

8. Notwithstanding this narrow definition, this does not appear to be an intended outcome. The OECD Guidance, when describing a securitisation entity, explicitly

recognises at paragraph 9 on page 140 that the "precise form of the cash extraction mechanism varies depending on the structure", and at paragraph 10, it acknowledges that such vehicles "only make a negligible profit (at most) over the life of the transaction, **after taking into account the impact of the cash extraction mechanism**. This is because the cash extraction mechanism will require surplus cash to be paid out to the originator (or another Constituent Entity in the same MNE Group as the originator). **Thus it appears that the OECD is cognisant of the varying ways in which securitisation entities are structured, and it appears to be an oversight that the definition has been so narrowly cast**.

9. Given that the OECD definition is inappropriate for the Australian market, and there is already a well-understood definition being widely applied in section 820-39, we submit this definition should be adopted. As a practical matter, there are (at the very least) many hundreds of securitisation vehicles currently in existence which will have been tested against the definition in section 820-39. If a new definition is adopted, it would be necessary to undertake due diligence to determine whether all such vehicles satisfy the new definition, which would result in an excessive burden on industry, for no real benefit. This would increase the costs faced by industry, which would ultimately be borne by end customers (such as the borrowers under ordinary residential mortgages).

Suggested legislative amendments

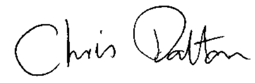
1. We suggest that section 20 of the Assessment Bill, which sets out the definition of *Excluded Entity*, should be amended to include an Entity which meets the conditions in section 820-39(3) of the *Income Tax Assessment Act 1997* (Cth). This amendment would exclude qualifying Australian securitisation vehicles from being Constituent Entities of an MNE Group, and thus from any computation of GloBE Income or liability for Australian top-up tax.

2. Importantly, we note that extending the definition of *Excluded Entity* to include an entity satisfying 820-39 of the 1997 Act will not exclude equity distributions made by a securitisation vehicle to Constituent Entities of an MNE Group from contributing to the GloBE Income of the MNE Group. While the securitisation vehicle, as an Excluded Entity, would itself be excluded from contributing GloBE Income to the MNE Group, equity distributions will be made to relevant unit holders within the MNE Group (this being the cash extraction mechanism for such vehicles) and will therefore contribute to the GloBE Income of the MNE Group.

3. Alternatively, securitisation entities could be retained within the scope of the DMT, and their GlobE income included in the MNE Group's income, so long as any liability referable to the securitisation entity's GloBE income was allocated to the entities holding equity interests in the securitisation entity.

We look forward to discussing your views on the contents of this letter when we next meet on Thursday 1 August.

Yours sincerely,



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