

## Media Release – Henry Tax Review

**FOR IMMEDIATE RELEASE**

### **Henry recommendations on savings and offshore funding a boost for banks: Deloitte**

**Monday 3 May 2010:** The Henry Review has recommended the introduction of a personal savings income discount of 40% on interest income from bank deposits. This will also cover residential rental income, capital gains and interest expense on listed share investments. In addition, the Henry review has recommended a broadening of the exemption for interest withholding tax on funds raised by banks operating in Australia from offshore sources which is consistent with one of the recommendations of the Australian Financial Centre Forum chaired by Mark Johnson

“If the Government adopts these recommendations they are likely to have a positive effect on the funding strategies of Australian banks over the longer term,” said Deloitte Banking Tax Services partner Emanuel Hiou.

The Government indicated that the recommendations on incentives to improve savings will be considered further in the coming months and form part of a second term agenda.

“These proposals will enable Australian banks to diversify their funding sources, address a significant funding gap between customer loans and deposits and provide them with access to potentially lower cost funding.

“Ultimately, this should enable banks in Australia to offer more competitively priced products and make it easier for customers to access funding. Foreign banks operating in Australia may also be able to offer more competitively priced funding products to customers in Australia as they will potentially be able to source funds from offshore related entities free of withholding tax,” said Hiou.

Hiou pointed out that the Global Financial Crisis reinforced that Australian banks have an uncomfortable reliance on wholesale funding, particularly from foreign markets. Through the global crisis Australian banks continued to access the wholesale funding markets (with the Government’s guarantee in many cases) to refinance maturing debt and increase liquidity. Where possible the higher costs on this funding were passed on to customers.

“As the global banking system and economies emerge from the GFC, Australian banks have been reviewing their funding strategies with the objectives of diversifying their funding sources, exploring opportunities to access lower cost funding and enhancing their liquidity management,” said Hiou.

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“This has included strategies to increase the size of the banks’ deposit base from both Australian and offshore customers.

“If the Government adopts these recommendations, they will go a long way to enabling Australian banks to meet these objectives.

Hiou explained that Australian banks have historically had a strong reliance on wholesale funding and a large proportion of this funding is sourced from foreign markets.

“This reliance has arisen, in part, from the low level of funding Australian banks are able to access from customer deposits,” he said. “Over the years as Australian banks have experienced strong growth in business and household lending, due to a strong and resilient domestic economy, the funding gap between customer lending and deposit growth has widened substantially. This has led to an increased reliance on wholesale funding to meet this gap,” Hiou explained.

Australian banks have one of the lowest customer deposit ratios globally - measured as customer loans to deposits.

“While Australian banks have been able to increase the size of their deposit base mainly through competitive pricing over the past 18 months the funding gap is still quite significant,” Hiou said.

“While Australian banks are able to structure their offshore wholesale funding programs to qualify for the existing interest withholding tax exemption, there are currently some potential sources of funding which do not qualify for the withholding tax exemption or double tax treaty relief,” he said. “This mainly relates to funding from offshore private retail investors in Asian and European countries and the United States.

“Under the existing withholding tax regime, Australian banks seeking to access funding from such investors have often been forced to wear the withholding tax or wear relatively expensive funding.

“On this basis this funding source has been very limited for Australian banks and these mooted recommendations on incentives to improve savings will be very welcome,” said Hiou.

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