Islamic Finance in Australia
Interest or not interest, that is the question?

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MOVING THE WORLD TO ISLAMIC BANKING

RETAIL, CORPORATE, INVESTMENT, ASSET MANAGEMENT, CORPORATE FINANCE, TREASURY
Islamic Finance: Australia reacts belatedly. And impetuously?

Introduction

➢ The growth of Islamic Finance

➢ The Shariah

➢ The prohibitions

➢ The structures

➢ The tax implications

➢ The opportunity

➢ The Australian response
KEY PRINCIPLES UNDERLYING ISLAMIC FINANCE

- Prohibition of riba
- Prohibition of uncertainty
- Profit sharing and risk sharing
- Prohibition of forbidden assets (e.g., alcohol, gambling)
- Existence of an underlying asset
The *Shariah* and finance structures

- *Murabaha* (cost plus)
- *Mudharabah* (profit sharing limited partnership)
- *Ijara wa-igtina* (lease-purchase)
- *Musharakah* (joint venture) and *sukuk* (securitization)
MURABAHA MECHANISM

Bank

Sale for deferred payment 110

Party A (customer)

(a) Goods retained for own use
Cost 110

OR

(b) Sale for immediate payment
Sale 100
Cost 110

Goods supplier

Goods buyer

Source: PwC UK
MUDARABA MECHANISM

Investor

Cash investment

Agreed share of profits
Investor bears losses

Mudarib

Manages

Profits

Commercial Venture

IJARA SUKUK

Investors

Special Purpose Vehicle (SPV)

Owner

Issue Sukuk

Pay issue price

Periodical payments representing SPV's profits

Pay rent periodically

Sell building

Pay price

Lease

DIMINISHING MUSHARAKA TRANSACTION WITH 25 PER CENT DEPOSIT

Tax implications of Islamic finance

- Stamp duty
- GST/VAT
- CGT
- Income tax
Responses by other countries

- Malaysia
  - Positive discrimination

- United Kingdom
  - No special favours
Islamic finance in Australia

- Australian tax implications of Islamic finance
- Inward Islamic foreign investment
- Developments in Australia
  - 2004 Victorian stamp duty amendments
  - 2009 Financial Centre Forum report
  - 2010 Australian Trade Commission report
  - 2010 Board of Taxation Discussion paper
Critique of the Australian response: threshold questions

- In substance interest or in lieu of interest?
- Should Australia cater for Islamic finance?
  - The Islamic interest / The national interest
- Are reforms benefitting one religious group permissible?
- Should artificial / complex financial arrangements be endorsed?
Critique of the Australian response: threshold questions (cont’d)

- Are tax concessions a desirable policy tool?
- Acceptability of tax integrity risks?
- How significant is Islamic finance?
- Is tax important to Islamic financiers?
- `Level playing field` concession or global finance centre?
Conclusion

➢ Reform process failure?