

Circular To: All Members

346/99

GST ON DELIVERABLE COMMODITY FUTURES CONTRACTS

The Board of the Exchange resolved on 16 December 1999 to change the contract specifications for the following contract months so as to facilitate the quoting of bids and offers at prices which *exclude* Goods and Services Tax:

Wheat	-	March 2001 and subsequent months
Greasy Wool	-	April 2001 and subsequent months

The effect of the changes to be made to the relevant By-Laws will be to require the buyer to pay an additional 10% to the seller on top of the daily settlement price at delivery, after calculation of any premiums or discounts.

For both Wheat and 21 micron Wool, there will be four contract months that will continue to be priced on the basis that the traded price *includes* GST (i.e. that the buyer is *not* required to top up the settlement value, determined in accordance with the existing By-Laws, by an amount attributable to GST). They are:

Wheat	-	July 2000	September 2000
		November 2000	January 2001
Greasy Wool	-	August 2000	October 2000
		December 2000	February 2000

Further explanation of the rationale for adoption of this dual approach is attached. Any queries in relation to this announcement can be directed to the undersigned by phone: 02 9256 0400, fax: 02 9256 0666 or email: mstarr@sfe.com.au

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GST on Deliverable Commodity Futures Contracts

This document elaborates on the decision taken by the Board of the Sydney Futures Exchange on 16 December 1999 relating to the pricing and settlement of commodity futures contracts that are subject to GST on deliveries.

The following table indicates, by reference to the month in which the contract expires, whether GST is treated as being included in the quoted price for SFE contracts.

Wheat Futures	July 2000 to January 2001 GST – Inclusive	March 2001 and subsequent contract months GST – Exclusive
Greasy Wool Futures	July 2000 to February 2001 GST – Inclusive	April 2001 and subsequent contract months GST – Exclusive
All other futures and options contracts ¹	July 2000 and subsequent contract months No GST (Input Taxed)	

Terms used in Table

GST – Inclusive Traded price is treated as including GST. Seller pays GST out of settlement amount. This is calculated by reference to daily settlement price (no change to existing By-Laws).

GST – Exclusive Traded price is treated as not including GST. A buyer that takes delivery will effectively pay GST when paying the seller an additional 10% on top of the price calculated by reference to daily settlement price. (Seller retains legal liability for paying GST to the Tax Office out of amount received from buyer).

No GST / Input Taxed No GST is payable by either party on the value of the contract (Although GST may arise in respect of commission charged for broking services associated with supply of such contracts). The contract is an input taxed “financial supply”.

¹ This includes:

- a) all financial futures (whether deliverable or cash settled) and options over financial futures;
- b) deliverable wool and wheat futures contracts that are closed out prior to expiry;
- c) 19 and 23 micron wool futures contracts (which are cash settled).

Pending clarification from Australian Taxation Office, status of options over deliverable wool and wheat futures contracts remains unclear. The Exchange will notify the market as soon as this is clarified.

Examples

The following examples indicate how settlement procedures / invoicing will vary under “GST-inclusive” versus “GST-exclusive” approaches:

GST Inclusive

Trade Date:	Say, 1 October 1999 (or other date <i>prior</i> to SFE changeover announcement of 17 December 1999)
Contracts:	8 Wheat Futures Contracts for delivery in “GST-inclusive” period from July 2000 to January 2001.
Daily Settlement Price at Expiry:	\$174 per tonne
Location Discount:	\$25.50 per tonne
Net Receipt by Seller:	\$148.50 per tonne X 8 contracts (at 50 tonnes per contract) = \$59,400
Invoicing:	Clearing House to issue invoices to the clearers for each party indicating that the final settlement amount includes GST of \$5,400, being one eleventh of \$59,400

GST Exclusive

Trade Date:	Say, 1 February 2000 (or other date <i>after</i> SFE changeover announcement of 17 December 1999)
Contract:	1 Greasy Wool Futures Contract for delivery in “GST-exclusive” period from April 2001 onwards
Daily Settlement Price at Expiry:	790 cents per kg
Total of Premiums and Discounts:	40 cents per kg discount
Net Receipt by Seller:	750 cents per kg plus 75 cents GST per kg multiplied by , say, 2580 kg = \$21,285 ²
Invoicing:	Clearing House to issue invoices to the Clearers for each party indicating that the final settlement amount includes GST of \$1,935, being 75 cents X 2580 kg.

² In the event that wool tax were payable by the seller, being the first time that that wool has been sold, the clearing house would deduct wool tax of 4% of the settlement amount *before* GST, i.e. 4% of 750 cents per kg, in the above example.

Q: *What is the background to this decision to switch over to “GST-exclusive” pricing for new contract months?*

A: Market participants were advised by the Exchange in September 1999 (Circular No. 268/99 of 22/9/99) that the terms of existing contracts would not be altered so as to deem them to have been entered at “GST-exclusive” prices.

This decision to persist with “GST-inclusive” pricing was made necessary by the Government’s failure to clarify the precise GST treatment of deliverable futures contracts until long after futures contracts for July 2000 and subsequent deliveries had commenced trading. (Only by August / September 1999 was it becoming clear that GST would be payable in respect of deliverable contracts).

Adoption of “GST-exclusive” pricing for July 2000 futures contracts would have necessitated changes to the terms of contracts after they had been entered. This raised the prospect of the Exchange being party to altering the rules that market participants needed to take into account when attempting to determine the impact of the Government’s decisions, assumptions upon which parties had traded.

To avoid this outcome, the Exchange announced that it would not be amending the By-Laws. Instead, it simply reminded participants of the consequences of the Exchange having made no amendment: if market participants did not make provision for GST in their pricing, sellers who allowed their contracts to expire would effectively bear the cost of GST rather than being able to charge it to the buyer.

If underlying forward prices were consistently being quoted on a “GST-inclusive” basis *and* the seller’s liability for GST were calculated by reference to the price at which the seller had *traded*, (rather than settlement price) there would be a case for “GST-inclusive” pricing of deliverable futures contracts continuing indefinitely.

However, on 20 October 1999, the Government made regulations clarifying the GST treatment of various “financial supplies”. Those regulations included a clarification of the basis upon which GST on deliveries pursuant to wool and wheat futures contracts would be calculated. They provided that the seller’s liability is to be calculated by reference to the daily *settlement price* (after calculating any premiums or discounts) at the time of delivery (and not by reference to the original traded price).

As a result, parties are unable to accurately price the GST component when entering a deliverable futures contract. This unsatisfactory outcome cannot be avoided in respect of contracts that are currently available for trading and in respect of which there are open positions. (Those holders of open positions entered the contract on the basis that they needed to factor GST into the pricing).

However, for all contracts in which there are no open positions, there is scope to accommodate the Government’s clarification by ensuring that everyone starts pricing contracts on a “GST-exclusive” basis. The first contract months in which “GST-exclusive” pricing can be adopted are March 2001 for wheat and April 2001 for wool.