
Managed investment trust withholding regime for foreign pension funds

Outline of chapter

1.1 Schedule # of this Exposure Draft Bill amends the *Income Tax Assessment Act 1997* (ITAA 1997) to ensure that foreign pension funds can access the managed investment trust (MIT) withholding tax regime and the associated lower rate of withholding tax on income from certain Australian investments.

Context of amendments

1.2 The MIT withholding tax regime provides a reduced rate of withholding tax for foreign investors in Australian managed funds for the purposes of attracting and retaining foreign investment in Australia.

1.3 Broadly, the liability for MIT withholding tax is imposed on foreign residents in respect of the fund payments they receive either directly or indirectly from a MIT.

1.4 However, under the current law, the concessional MIT withholding tax does not apply in circumstances where an ultimate beneficiary cannot be established. This will occur where fund payments are made to a trust without presently entitled beneficiaries.

1.5 In effect, this means that a foreign pension fund, as a foreign beneficiary or foreign custodian, will not have access to the MIT withholding tax regime if it receives fund payments as a trustee and does not have beneficiaries that are presently entitled to the payments. Instead, the foreign pension fund may be liable to tax under the general provisions relating to the taxation of trusts in Division 6 of Part III of the *Income Tax Assessment Act 1936* (ITAA 1936) and may be taxed at the highest marginal tax rate.

1.6 These amendments will ensure that foreign pension funds can access the MIT withholding tax regime and the associated lower rate of withholding tax on eligible Australian investments.

1.7 The amendments will apply to income years commencing on or after 1 July 2008. This application date will ensure that affected foreign pension funds can access the MIT withholding tax regime as originally intended; it will also reflect current industry practice.

1.8 These amendments have been actively sought by the Australian funds management industry and are beneficial to affected foreign pension funds.

Summary of new law

1.9 Schedule # of this Exposure Draft Bill amends Division 840 of the ITAA 1997 to ensure that foreign pension funds can access the MIT withholding tax regime. Under the amendments, foreign pension funds will be treated as the final beneficiary of a fund payment and will be liable for MIT withholding tax.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
Fund payments made to foreign pension funds will be subject to the MIT withholding tax regime.	Fund payments made to foreign pension funds may be subject to the general trust taxation rules.

Detailed explanation of new law

1.10 The MIT withholding tax regime provides a reduced rate of withholding tax for foreign investors in Australian managed funds for the purposes of attracting and retaining foreign investment in Australia.

1.11 Broadly, the liability for MIT withholding tax is imposed on foreign residents in respect of amounts received that represent, or are reasonably attributable to, the fund payments of a MIT.

1.12 These amendments ensure that a foreign pension fund that receives a fund payment as a trustee will be taken to be a beneficiary in its own right and, as a result, will be liable to income tax at the MIT withholding tax rate. *[Items 1 and 2, section 840-800 and subsection 840-805(4A)]*

1.13 A *foreign pension fund* is an entity that has the principal purpose of funding pensions (including disability and similar benefits) for the citizens or other contributors of a foreign country, provided that:

- the entity is a fund established by an *exempt foreign government agency* (as defined in the ITAA 1997), or is a *wholly-owned subsidiary* (as defined in the ITAA 1997) of such an entity;
- the entity is established under a *foreign law* (as defined in the ITAA 1997) for an exempt foreign government agency, or is a wholly-owned subsidiary of such an entity.

[Items 2 and 3, subsection 840-805(4B) and the definition of 'foreign pension fund' in subsection 995-1(1)]

1.14 As a foreign pension fund will be liable to income tax at the MIT withholding tax rate, a beneficiary of the fund that is presently entitled to a share of the income or capital of the fund will no longer be liable to MIT withholding tax. *[Item 2, subsection 840-805(4C)]*

Consequential amendments

1.15 Consequential amendments are made to the Pay As You Go withholding rules in Division 18 of Schedule 1 to the *Taxation Administration Act 1953* to ensure that the withholding tax regime, including the crediting provisions, apply appropriately. *[Item 4, subsection 18-32(3) in Schedule 1 to the Taxation Administration Act 1953]*

Application and transitional provisions

1.16 The amendments will apply to fund payments made in income years starting on or after 1 July 2008, the date when the MIT withholding tax regime commenced. *[Item 5]*

1.17 This will ensure that specified foreign pension funds can access the MIT withholding tax regime as originally intended and reflects current industry practice.

1.18 The amendments have been actively sought by the Australian funds management industry and are beneficial to affected foreign pension funds.

Amendment of assessments

1.19 Generally, the Commissioner of Taxation has the power to amend an assessment (including where a taxpayer requests an amendment) of a trust, other than a trust that is a small business entity,

within four years from the date of the notice of assessment. As these amendments may apply to income years in respect of which the four year amendment period has expired, the period for amending assessments will be extended. An assessment can be amended if:

- the assessment was made before the commencement of the amendments (that is, before the day on which the amendments receive Royal Assent);
- the amendment is made within two years after that date; and
- the amendment is made for the purpose of giving effect to these amendments.

[Section 4]