FSC FINANCIAL SERVICES COUNCIL

20 August 2015

General Manager
Small Business Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

Email: taxlawdesign@treasury.gov.au

Dear Sir/Madam

RE : IMPROVING TAX COMPLIANCE - ENHANCED THIRD PARTY REPORTING, PRE-FILLING AND DATA MATCHING

The Financial Services Council (FSC) represents Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advisory networks, licensed trustee companies and public trustees. The Council has over 125 members who are responsible for investing more than $2.5 trillion on behalf of 11 million Australians. The pool of funds under management is larger than Australia’s GDP and the capitalisation of the Australian Securities Exchange and is the third largest pool of managed funds in the world. The Financial Services Council promotes best practice for the financial services industry by setting mandatory Standards for its members and providing Guidance Notes to assist in operational efficiency.

The FSC fully supports Treasury and the Australian Taxation Office (ATO) with changes to improve tax compliance. We also support the moves toward increasing pre-filling and data matching for investors. We note that these objectives must be carefully balanced against the accuracy of this data and resulting taxation implications for investors.

The comments in our submission mainly relate to the provision of information regarding transfers of reportable securities and units in a unit trust. We have significant concerns about the industry’s capacity to comply with these new requirements in the stipulated timeframe.

The draft legislation contemplates capture of data from 1 July 2016, however the exact data fields and nature of information will not be finalised until the Spring sitting of Parliament, leaving very little time for reporters to be compliant.

While the draft legislation permits the Commissioner of Taxation to exempt certain entities or groups of entities from the reporting regime, we appreciate that it will take some time for the Commissioner to develop a consistent and fair set of rules in this regard. This will most likely leave reporters in a significantly uncertain regulatory environment as the commencement date approaches.

Further, the changes currently being developed in the new taxation regime for Managed Investment Trusts (the AMIT regime) are not finalised. These changes will have an impact on the cost base of units held in unit trusts and it is not possible to predict the full implications until such time as this regime is legislated in late 2015.

We feel there is a very likely possibility that the assumptions necessary to create pre-fill data will adversely affect investors. We understand from the ATO’s experience in listed securities that investors generally accept the assumptions made by the ATO about cost base and method (e.g.

FIFO etc). The cost base of units in a unit trust has many more variables than the cost base of listed securities and much of this information is not available to the trustee of the unit trust.

As a result we are concerned that the patchy and incomplete data which will be provided in the early years of the regime will produce unfavourable taxation outcomes for investors, which they will unknowingly accept – thus placing unit trust investments at a tax disadvantage to other investments (such as listed equities). This may also give rise to complaints and disputes from investors that subsequently identify the shortcomings with the data reported.

Moreover, the Attribution Managed Investment Trust (AMIT) regime will require significant systems changes for many operators at a time when additional reporting requirements are also being built for the United States' FATCA requirements, the OECD's Common Reporting Standard and the Australian government's MySuper and Stronger Super reforms. Significant resources are also being expended on developing Standard Business Reporting 2 capabilities for standardisation of electronic transactions from business to government (including SuperStream).

Even since the consultation on enhanced third party data reporting opened on 10 July 2015, an additional set of changes for the ATO's Annual Investment Income Report (AIIR v11) have been released for comment; further changes that directly impact unit trusts. The timing of these changes is particularly vexing given the forthcoming changes that will flow from the AMIT regime.

Together these regimes are placing the IT capability of members at maximum load. It is unclear how the regimes are intended to interact and there appears to be little acknowledgement of the potential for cross-over and duplication of effort. Members have indicated that lead times to start new systems projects are in excess of 18-24 months.

For these reasons we strongly recommend that the application of this regime to reportable securities and units in a unit trust is held off until the AMIT regime is legislated, SBR2 capabilities are further developed and other current reporting projects are completed.

Sufficient lead time needs to be provided from when the enhanced third party data reporting rules and associated ATO guidance are finalised. At least 18-24 months should be provided from finalisation to allow for necessary systems changes. Specifically, this deferral would apply to both Fund Managers and Third Party Trustees (such as IDPS/Wrap Operators and Custodians).

We have detailed our specific concerns and recommended changes in Appendix A, along with other issues which we would suggest require further consultations with Treasury and/or the ATO.

Should you wish to discuss this submission further please do not hesitate to contact me on (02) 9299 3022.

Yours sincerely

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Senior Policy Manager – Investment, Global Markets & Tax

Appendix A

Directly held interests in unit trusts

Members of the FSC are keen for there to be some flexibility about the reporting of investment into, and redemption of, units in unit trusts. Some members may wish to utilise existing CGT reporting and provide that to the ATO instead of altering their AIIR formats, others will prefer to alter the AIIR. It is noted that the legislation expressly allows the Commissioner to accept alternative reporting arrangements and we support this as it provides the necessary flexibility.

In the event that any members are able to comply with the first year reporting requires for 2016/2017, it is requested that any AIIR specification changes be circulated reasonably soon in order to enable adequate time to amend the underlying systems.

Clarification is also required as to the impact on AIIRs. Some managers lodge a composite AIIR for all of their trust offerings. Others lodge an AIIR for each trust. Under the new regime those lodging composite AIIRs will need to disaggregate the information in order to attach the details about new trust investments and redemptions.

Indirectly held interests in unit trusts

In some instances an interest in a unit trust is held indirectly either through a nominee company or through a Wrap service. This raises the question of who is to report on investments, divestments and redemptions. Is it the unit trust – who may not know who the true beneficial owner is behind the nominee company, or the Wrap service?

One solution might be that the primary obligation to report should rest with the organisation that has a direct relationship with the ultimate beneficial owner. To do otherwise would result in the nonsensical outcome of the unit trust reporting investment and redemption by a custodian / nominee which would be of very little utility. However in some instances the organisation with the direct relationship with the ultimate beneficial owner may not have access to the relevant data.

This issue is complex and members have not had sufficient time during consultation to be able to come to a conclusion on recommendations to government that would work appropriately in all situations. Further consultation and time is needed in this area and we suggest flexibility will be needed so that reporting can take the form of an AIIR or some other report if appropriate.

Ideally clarification as to who should bear the primary responsibility should be published sufficiently early (at least 18-24 months prior to commencement of reporting) so that relevant parties can identify the need for reporting and implement any necessary systems.

Payment systems

The electronic infrastructure involved within a payment system is complex and can include a number of different parties for one simple consumer transaction. In certain instances, discrete functions (e.g. switch capabilities) within a payment system can be outsourced.

The legislation is currently drafted in very broad terms, based on the definition within the *Payment Systems (Regulation) Act 1998* (Cth). In some instances, this may result in the ATO receiving the same income information about one taxpayer from multiple sources. The FSC requests that the Explanatory Memorandum be expanded to include further examples of which entities through a transaction payment cycle are required to report information.

The term “produces income for the business”, which a payment system administrator must report, is also a very broad term and does not rely on any consistent definitions within the Income Tax Assessment Acts, such as assessable income, ordinary income or statutory income.

Further, many payment system administrators may not know the nature of the income derived by the recipient.

The following examples highlight this issue:

1. A payment system administrator facilitates the payment of annual subscription fees through Bpay for a magazine provider. Clearly this income is intended to be captured within the policy of the legislation.

2. A payment system administrator facilitates the payment of deposit monies to a real estate agent for the sale of real property. The money is placed in a "regulated trust account" (under the respective state legislative scheme). It is unlikely that this income is intended to be captured within the policy of the legislation.

3. A payment system administrator facilitates the payment of residential rent to a real estate agent by all tenants through a Gateway payment service. The real estate agent takes a percentage of the rent roll as commission (i.e. assessable income) and the balance is then forwarded to the respective landlords. It is unclear whether this income, or part of it, is intended to be captured within the policy of the legislation.

We recommend that either an existing definition such as "ordinary income" be used with adequate safeguards regarding the knowledge of the payment system administrator, or that comprehensive examples be provided within the Explanatory Memorandum to give clarity to payment system administrators.

Market Participants/Brokers

Item 5 of s396-55(1) requires "market participants" (i.e. Brokers) to report transactions that result in a change to the type, name, number or value of reportable securities that are held by another entity.

In consultation meetings held during July and August 2015, representations were made by the Australian Taxation Office, explained within the Discussion Guide: Third Party Reporting For Sales of Shares and Units, that they will only be seeking Brokers to report "identity information" such as name, address, date of birth, origin of order and HIN/SRN.

While this ATO concession is fully supported by the FSC, the legislation allows no such flexibility, nor is there sufficient certainty within s396-65 (Exemptions) to allow Brokers comfort as to what data they must capture from 1 July 2016. As such, the FSC recommends that the wording in item 5 of s396-55(1) be amended to reflect the ATO's intention for data capture.

Timing of data reporting

The current timing of data reporting, 31 July is challenging. Currently, the due date for AIIR files is 31 October of each year, with many investment bodies requesting an extension from the ATO where they receive information from a third party such as a fund manager. Information for the new regime will likely come from the same or similar sources as the AIIR information. Therefore, we submit that the legislative due date of 31 July is impractical, or will result in significant underreporting of information if it remains.

While the draft legislation provides for the Commissioner to allow a later lodgement date, this does not provide any certainty or comfort in respect of this new reporting regime.

Other issues

Generally we feel there could be a more holistic approach to domestic and extra-territorial reporting requirements. We understand the need for transparency and fully support objectives of government in achieving pre-fill data on tax returns. However this needs to be balanced against existing government initiatives which are still being rolled out.

We ask that greater consideration be given to the cumulative impact of additional reporting projects that businesses are currently trying to implement. New reporting projects and initiatives appear to be progressed with little to no regard for concurrent projects that are collecting similar data through different mechanisms. We believe a more strategic approach that considered the interactions between these different regimes would be less costly and more manageable for business.

Further, there is no agreed framework to handle taxpayer complaints or disputes over pre-fill data provided to the ATO on behalf on investors. This is causing uncertainty and concern regarding potential litigation avenues that may become opened in the future. Again this area needs further consideration before this regime can be finalised.