NZSUPERFUND
Te Kaitiaki Tahua Penihana
Kaumātua o Aotearoa

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By email: stapledstructures@treasury.gov.au

31 May 2018

Dear Brendan

Stapled Structures –Reform Package

The Guardians of New Zealand Superannuation (**New Zealand Sovereign Fund - NZSF**) is submitting in relation to the first stage of Exposure Draft legislation and accompanying Explanatory Memorandum (*Treasury Laws Amendment (Stapled Structures and Other Measures) Bill 2018*) (the ED) giving effect to the Government's announced stapled structure reform package, released for comment on 17 May 2018.

We note that a second stage of Exposure Draft legislation and accompanying Explanatory Memorandum is expected to be released soon to deal with the agricultural Managed Investment Trust (**MIT**) changes and the conditions that stapled entities must comply with in order to access the infrastructure concession and/or transitional arrangements. We would like the opportunity to provide further consultation when this Exposure Draft legislation is released.

In this NZSF submission we comment on the aggregation of interests for the Sovereign Immunity exemption and the consistency of the transitional rules (particularly the deemed market value cost base reset) across the various components of the draft legislation.

Submission 1: Aggregation of interests for the Sovereign Immunity Exemption

The ED provides a framework for determining sovereign immunity and only exempts sovereign entities where they hold less than 10 per cent of an entity's ownership interest and do not influence an entity's key decision making[1]. The ED specifies that in order to test whether the 10 per cent threshold test is satisfied, a sovereign entity's interest in a particular entity must be aggregated with the interest of other sovereign entities from the same foreign country[2].

We are concerned with the notion of aggregating interests held by sovereign entities who are otherwise independent investment bodies from the same foreign country to determine whether or not the 10 percent safe harbour threshold has been exceeded. We submit that where a sovereign entity has a separate Board of Directors responsible for choosing the entity's investment mandate (and therefore the deployment of capital for each relevant investment) the 10 percent safe harbour threshold should be determined on an individual entity by entity basis. In the situation where a separate Board of Directors exists, we submit that there should be no aggregation of sovereign entity interests from the same foreign country.

To provide practical context to this issue and our experience we note the following:

[1] In accordance with the draft legislation, contained under proposed subsections 880-105(1)-(3) of the Income Tax Assessment Act 1997 (ITAA 1997). The draft legislation limits the exemption to trusts that are MITs in the relevant income year.

[2] Subsection 880-105(1)(d) of the ITAA 1997.

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- A foreign government may have established a number of sovereign funds for different purposes. In the case of New Zealand, the New Zealand Government has three Crown Financial Institutions (CFIs) that would meet the definition of sovereign entity (ie: the New Zealand Superannuation Fund, Accident Compensation Corporation and the Earthquake Commission). New Zealand Local (State) Government may have other funds that would also meet the definition of sovereign entity.

- All of the New Zealand sovereign entities have separate Boards of Directors and investment mandates. None of them are influenced, directed, controlled or subject to the instruction of any other sovereign entity (or any single, central authority in New Zealand).

- It would not be feasible to definitively determine whether or not the New Zealand Government exceeded the 10 percent threshold when aggregating the investments held across the separate sovereign entities from time-to-time. Other than in the rare situation where they were co-investing together in a particular entity, individual sovereign entities would not be aware of what investments the other CFIs had made nor would they have any awareness of investments made by local government funds be they in listed or unlisted entities / vehicles.

We submit that the 10 percent safe harbour threshold should be determined on an individual entity by entity basis where a sovereign entity has a separate Board of Directors responsible for choosing their own investment mandate. There should be no aggregation of foreign government interests in this situation.

Submission 2: Deemed market value cost base reset for agricultural MITs

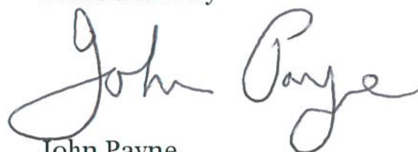
The ED provides that existing investments of a sovereign entity that would otherwise not qualify for sovereign immunity under the proposed new law[3], but will benefit from the transitional rules, will have the cost base of its pre-27 March 2018 investments reset to market value at the end of the transitional period[4].

We submit that a similar approach should be adopted for the drafting of the agricultural MIT legislative changes. This would mean that existing agricultural MIT investments that would otherwise not derive concessional MIT income (or eligible investment business income) under the proposed new law, but will benefit from the transitional rules, should have the cost base of such investments reset to market value at the end of the transitional period[5].

In circumstances where a MIT continues to hold a transitional investment in agricultural land and disposes of it after the transition period, it would be appropriate to limit the rate of tax on any accrued capital gain at the end of the transitional period to 15% – with any subsequent accretion in value subject to tax at the higher corporate tax rate. The gain would be taxed on disposal of the asset. We submit that this provides an equitable outcome for taxpayers in respect of the taxation of unrealised gains that had accrued before a change in taxation policy was introduced.

Please contact me if you have any questions or require any clarification ([redacted] or [redacted].

Yours sincerely



John Payne
Head of Tax

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[3] Subsections 880-105(1)-(3) of the Income Tax Assessment Act 1997 (ITAA 1997).

[4] Subsection (2)-(4) of *Schedule 4 Sovereign Immunity – Part 2 Application and transitional provisions, (5) Transitional – deemed sale and purchase.* In accordance with subsection (4), the end of the transitional period will be the day the later of 1 July 2026 and the day before the private ruling (applying to the sovereign entity) ceases to apply.

[5] Including having the cost base of beneficiaries interest in the relevant agricultural MIT reset to market value at the end of the transitional period.