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Market Conduct Division
Treasury
Langton Cres
Parkes ACT 2600

Email: CIVreform@treasury.gov.au

Dear Sir/Madam,

Corporate Collective Investment Vehicles (CCIV): Tax Framework

The Australian Custodial Services Association ("ACSA") appreciates the opportunity to provide this submission to Treasury on the legislation and related explanatory materials that implement the tax components of the CCIV regime.

About ACSA

ACSA is the peak industry body representing members of Australia's custodial and investment administration sector. Collectively, the members of ACSA hold securities and investments in excess of AUD $4 trillion in value in custody and under administration. Members of ACSA include NAB Asset Servicing, JP Morgan, HSBC, State Street, BNP Paribas Securities Services, Citi and Northern Trust.

Support for the CCIV regime

ACSA supports the introduction of the CCIV regime as a way of increasing the competitiveness of the Australia's managed funds industry through the introduction of an internationally recognisable investment structure. ACSA is, however, concerned that the CCIV regime, as currently drafted, may not achieve this objective because Australia's complex withholding tax regime for trusts could deter investment in CCIVs with investors preferring alternative UK, Europe and Asia structures that provide more attractive and simpler tax settings.

In order for the CCIV regime to increase the competitiveness of the Australia's managed funds industry, ACSA believes that the issues outlined below should be addressed.

Withholding tax

The draft legislation deems the assets, liabilities and business referable to a sub fund to be trusts for Australian tax purposes. Accordingly, the withholding tax regime that currently applies to trusts will be extended to CCIVs under the draft legislation.

Australia's complex non-resident withholding tax regime places Australian funds at an immediate disadvantage in a global context and when compared against the counterparts in the UK, Europe and Asia. The removal of tax complexity for non-resident investors could strengthen Australia's international competitiveness and contribute to the expansion of Australia's financial services into the Asian region. We are concerned that the treatment of sub funds as trusts without any simplification of the withholding tax regime will not achieve this.

The key factors that contribute to the complexity of Australia's non-resident withholding tax regime include:

- Different tax treatment of various forms and types of income
- Different tax rates applicable to each category of income
- Bilateral Tax Treaties and Tax Information Exchange Agreements (TIEA) that impose different rates between countries
- Different basis for determining applicable WHT rate – dividends and interest – tax residency of ultimate beneficial owner, fund payments – address of payee.
- Withholding on certain deemed payment amounts
- The requirement to addback capital losses from non-taxable Australian property in the calculation of fund payments.

As outlined above, different tax treatment of various forms of income and different tax rates contribute to the complexity of Australia's non-resident withholding tax regime. Bilateral tax treaties including the Tax Information Exchange Agreements (TIEA) add further complexity by imposing different tax rates for the same category of income for tax residents of different countries.

The withholding on deemed payments, and the requirements to add back capital losses from non-taxable Australian property when calculating fund payments introduces another level of variation in taxing approach of the non-resident investors. ACSA notes that there is a divergence and a level of uncertainty in the industry with the way these requirements are applied. As a result, these requirements are particularly difficult to explain to potential and actual investors and withholding tax may be imposed on amounts in excess of the commercial returns from these investments.

The application of these rules in practice means that various income types paid to the non-resident investors such as dividend, interest, royalty and the fund payments each attract different tax rates determined by the tax residency status of the ultimate beneficial owner or the address of the payee. Further, in respect of fund payments, different rates may apply to the extent some or all of the fund payment is attributable to

Non-Concessional Managed Investment Trust (MIT) income or Clean Building MIT income.

A non-resident investor considering investing into Australian market who may not necessarily understand the Australian taxation law will find it difficult to navigate through the complex taxation maze and determine the tax impost on their investments. In fact, the tax consequence can only be understood when the distribution is paid or deemed to be paid and broken down into income components. This could deter investment in Australian funds with investors preferring alternative investments that provide more attractive and simpler tax settings.

Additionally, the numerous trust types, income categories and investor status permutations that arise add immense complexity in administering the withholding taxes. This complexity results in material costs and compliance risks being incurred by businesses to comply with the regime, which in turn could limit the appetite for innovation by issuers and service providers.

Tax treaties

The OECD Model Tax Convention on Income and Capital, which is the basis upon which bilateral tax treaties are modelled, defines a company as, in the first place, any body corporate. In addition, the definition of company includes any other taxable unit that is treated as a body corporate according to the tax laws of the contracting state in which it is organised.

At paragraph 1.97 of the Exposure draft explanatory materials, it is the intention that:

> *a CCIV sub-fund trust and its beneficiaries are eligible for the same treatment, and are able to access the same benefits, as an AMIT under Australia's double taxation agreements.*

A CCIV is a legal form company, however it is deemed to be a trust for Australian tax purposes. ACSA submits that this could cause confusion amongst some jurisdictions and it may be open for some jurisdictions to determine that a CCIV fits the definition of company for treaty purposes.

Residents of that jurisdiction may therefore expect to access the treaty withholding tax rate on dividends, which is in most cases is capped at 15%.

As mentioned in the section above, Australia's withholding tax regime is complex. Withholding on deemed payments and the requirement to add back capital losses on non-taxable Australian property when calculating fund payments can cause the effective rate of withholding tax on dividends to be higher than 15%, meaning that the tax treaty has been contravened.

The examples below illustrate this anomaly:

Example 1 Withholding tax on deemed payments

		$
Dividends paid by CCIV as per distribution statement		100
Withholding tax as per the treaty rate (15%)		**$15.00**
Non-resident section of AMMA statement	Cash	Attribution
	$	$
Unfranked dividend	100	100
Deemed payment – unfranked dividend		50
Total		150
Withholding tax payable under domestic Australian tax law (15%)		**$22.50**

The withholding tax payable under Australian tax law exceeds the withholding tax payable under the treaty by $7.50.

Example 2 addback capital losses on non-taxable Australian property when calculating fund payments

	$
Dividends paid by CCIV as per distribution statement	100
Withholding tax as per the treaty rate (15%)	**$15.00**
Capital gains on Taxable Australian property	500
Less Capital losses on non-Taxable Australian property	400
Net capital gain	**100**
Dividends paid by CCIV per distribution statement	100
Fund payment calculation:	
Net capital gain	100
Add back capital losses on non-Taxable Australian property	400
Capital gains on Taxable Australian property	**500**
Fund payment	500
Withholding tax payable under domestic Australian tax law (15%)	**$75.00**

The withholding tax payable under Australian tax law exceeds the withholding tax payable under the treaty by $60.00.

In the interests of providing transparency for foreign residents who are considering investing in a CCIV, ACSA recommends that the Explanatory materials for the final legislation contain worked examples that demonstrate how domestic Australian withholding tax will be applied, including the scenarios above.

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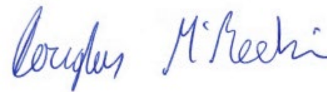
The comments in this letter do not comprise financial, legal or taxation advice and should not be regarded as the views of any particular member of ACSA. We will be pleased to discuss this submission with you or arrange a meeting with our members to obtain further feedback.

Please contact the Chair of ACSA's Tax Working Group, Duncan Lyon on 0414 566154 or Deputy Chair, Doug McMeekin on 0436 683759 to discuss any of the issues raised in this letter.

Yours faithfully,



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