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SUBMISSION

Submission to Treasury: Expanding Australia's tax treaty network

29 October 2021

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29 October 2021

Dear Sir/Madam

Expanding Australia's tax treaty network

The Association of Superannuation Funds of Australia (ASFA) is pleased to provide this submission in response to the Treasury consultation on expanding Australia's tax treaty network.

About ASFA

ASFA is a non-profit, non-political national organisation whose mission is to continuously improve the superannuation system, so all Australians can enjoy a comfortable and dignified retirement. We focus on the issues that affect the entire Australian superannuation system and its $3.3 trillion in retirement savings. Our membership is across all parts of the industry, including corporate, public sector, industry and retail superannuation funds, and associated service providers, representing almost 90 per cent of the 17 million Australians with superannuation.

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If you have any queries or comments in relation to the content of our submission, please contact Julia Stannard, Senior Policy Advisor, on (03) 9225 4027 or by email jstannard@superannuation.asn.au.

Yours sincerely

Julian Cabarrus
Director - Policy Operations, Member Engagement & External Relations

General comments

ASFA welcomes the Consultation aligned with the expansion of Australia's double tax treaty network aimed at stimulating economic integration through foreign investment and trade. This is particularly important to the superannuation industry, which represents some of the largest Australian investors in foreign jurisdictions.

The removal of or reduction in taxation barriers caused by double taxation of income or capital gains will assist the industry in its primary objective to advance the retirement outcomes for Australians.

ASFA's submission has been prepared with the assistance of our Tax Specialist Advisory Committee. The Committee has identified several matters that ASFA considers should be addressed in relation to Australian superannuation funds when Australia enters into new tax treaties or renegotiates existing treaties.

ASFA's primary concerns, as part of the expansion of the treaty network, are to ensure:

- a consistent definition of 'pension scheme' or 'superannuation fund' is adopted into Australia's tax treaties
- there is clear recognition of Australian superannuation funds as 'persons' or beneficial owners for treaty purposes
- treaties to which Australia is a party specifically exempt the income of an Australian superannuation fund from tax in the other country
- lump sum payments from Australian superannuation funds are appropriately treated as subject to withholding tax at source (that is, in Australia)
- any updated treaty between the United States (US) and Australia addresses the US tax consequences of income accrued, other gains or accretions, contributions to and distributions from Australian superannuation funds to US persons.

ASFA provided a submission in 2016 to the OECD in relation to a discussion draft on the 'treaty residence of pension funds'. That submission, a copy of which was made available to Treasury at the time, confirmed our view that greater clarity in the residency status of Australian superannuation funds would assist in removing or reducing taxation barriers caused by double taxation of income or capital gains derived by such funds, and thus would assist the entire Australian superannuation industry in its primary objective to advance the retirement outcomes for Australians. We have provided a copy of our 2016 submission for your consideration alongside this submission.

Specific comments

1. Consistent definition of 'pension scheme'/'superannuation fund'

ASFA submits that insertion of a consistent definition of an Australian superannuation fund into Australia's treaties would assist greatly with the application of treaties and therefore the facilitation of the global investment of Australian superannuation funds.

Despite the significant growth of the Australian superannuation industry, there are many jurisdictions that Australian superannuation funds invest in, that have a varied understanding of the purpose and legal form of Australian superannuation funds. This causes impacts including time delays, cost and complexity for Australian superannuation funds, and is further exacerbated as the tax treaties between countries fail to define an Australian superannuation fund or fail to define it adequately and consistently.

An example of where a superannuation fund is well defined is included in the Swiss Confederation-Australia treaty in Article 3, paragraph 1(i):

> *(i) The term "pension scheme' means any plan, scheme, fund, foundation, trust or other arrangement established in a Contracting State or, in the case of Australia, that is an Australian superannuation fund for the purpose of Australian tax, which is:*
>
> *(i) regulated by that State; or*
>
> *(ii) operated principally to administer or provide pension or retirement benefits or to earn income for the benefit of one or more such schemes.*

The Swiss Confederation-Australia treaty is the only Australian treaty ASFA is aware of that incorporates a specific definition of an Australian superannuation fund.

Consistent with the accompanying ASFA submission from 2016, ASFA also submits that a definition of 'pension scheme' or 'superannuation fund' would be most effective for Australian funds if it also included those entities wholly owned by Australian superannuation funds (see item (d), page 6 of the 2016 submission).

Recommendation
A consistent definition of an Australian superannuation fund should apply
A consistent definition of an Australian superannuation fund should be included when negotiating tax treaties with other countries, and/or renegotiating or liaising with jurisdictions in respect of existing tax treaties.

2. Australian superannuation funds as 'persons' or beneficial owners for the purposes of double tax treaties

For many of ASFA's large superannuation fund members, one of the more significant practical issues with Australia's tax treaties is that a number of jurisdictions are not willing to accept that Australian superannuation funds are beneficial owners of income entitled to treaty benefits. As a result, these jurisdictions do not accept a Certificate of Residency from the Australian Taxation Office (ATO) as sufficient documentation to enable a superannuation fund to claim the benefits of the treaty. The legal form of Australian superannuation funds as trusts causes additional uncertainty, particularly in non-common law jurisdictions, such as Spain, that have historically not recognized the concept of trust in their laws.

For example:

- absent a detailed confirmatory formal tax ruling application process, Taiwan takes a "look through" approach to establishing the beneficial owners of the income and requires Australian superannuation funds to provide additional, detailed and extensive documentation in respect of funds' underlying members. It may be appreciated that, unless the quantum of dividend income from these jurisdictions is very large, the compliance costs in obtaining this documentation may easily outweigh the potential benefits from the application of the lower withholding tax rate specified in the treaty.
- Korea requires superannuation funds to certify that they are "pension funds set up under the laws of a treaty partner country that are similar to Korean laws on pension funds". Due to the complexity of pension and superannuation fund laws in both jurisdictions, it may not be possible to establish this to the satisfaction of the Korean authorities in the absence of a lengthy and complex confirmation process.

In addition, Australian income tax legislation operates such that, strictly, the maximum foreign income tax offset (FITO) is limited to the treaty rate (even if in practice, this treaty rate is difficult or very costly to obtain). This means that no FITO is available for any withholding tax that exceeds the treaty rate. In these circumstances, the Australian superannuation fund actually incurs *higher* total taxes on dividend income from these jurisdictions than on the equivalent dividend income from a jurisdiction with which Australia has no treaty. This is because, in the case of dividends from a non-treaty country, it is likely the FITO would be available for the full withholding tax imposed, provided that the Australian superannuation fund had not exceeded its FITO cap in respect of its total foreign income.

Finally, as a practical matter, while a number of Australia's treaty partner countries — including Switzerland (see above in section 1) — may observe the reduced treaty withholding rates for Australian superannuation funds, in practice they do not apply those reduced treaty rates at the point of payment (at source). This leaves superannuation funds in the position of having to retrospectively apply to have excess withheld amounts above the treaty rate refunded from the relevant tax authorities. The documentation required to be submitted to accompany the 'reclaim' application varies and can often require certification from the ATO. This causes the superannuation fund to incur time delays and costs.

Recommendation

Key outcomes for tax treaties

In negotiating tax treaties with other countries, and/or renegotiating or liaising with jurisdictions in respect of existing tax treaties, key outcomes should include:

- any agreed withholding tax rates pursuant to the treaty should apply to all dividends paid by a resident of that country to an Australian person, and an Australian superannuation fund should be specifically included to be treated as an 'Australian person' for that purpose
- the agreed withholding tax rates should apply at the point of payment of the dividends by companies resident in the other jurisdiction, and not require the Australian person to apply for refund or reclaim of an initially over-withheld amount from the revenue authorities in the other jurisdiction
- if the other jurisdiction requires documentation to evidence that an Australian superannuation fund shareholder is an Australian person, such documentation be limited to a Certificate of Residency obtained by the Australian superannuation fund from the ATO (without any additional specification in respect of the percentage of the fund's Australian-resident members).

3. An exemption from tax on an Australian superannuation fund's income in foreign jurisdictions

ASFA notes that paragraph 69 of Article 18 of the OECD Model Treaty contemplates the inclusion of a specific exemption for a pension fund in one country from tax on its income in the other country. The OECD commentary seems to limit this to circumstances where both countries do not tax pension fund income (unlike Australia, which taxes most superannuation fund income at 15%).

However, the relatively low rate of taxation of superannuation fund income in Australia means that many of the same issues that gave rise to the need for an exemption for pension funds (that is, taxation in one country, without the capacity to provide adequate credit for such tax in the other country) are also relevant to Australia.

Accordingly, there would seem to be no compelling reason why Australia should not seek to include an exemption in its treaty negotiations. Indeed, ASFA notes that Australia already provides exemption from withholding tax in paragraph 128B(3)(jb) of the *Income Tax Assessment Act 1936*, as amended, in all circumstances where the relevant income is exempt in the foreign jurisdiction.

ASFA submits that an exemption for Australian superannuation funds could be modelled on exemptions included in a number of the UK's double tax treaties, which are typically included in the Article of the treaty dealing with dividend income. ASFA notes that, typically, withholding tax on dividends accounts for the largest single part of the foreign tax paid by pension funds, including by Australian superannuation funds.

By way of examples, extracts from the UK-Switzerland and UK-Japan treaties follow:

UK-Switzerland treaty

However, such dividends:

(a) shall be exempt from tax in the Contracting State of which the company paying the dividends is a resident if the beneficial owner of the dividends is:

(i) a company which is a resident of the other Contracting State and controls, directly or indirectly, at least 10 per cent of the capital in the company paying the dividends; or

(ii) a pension scheme;

UK – Japan treaty

Notwithstanding the provisions of paragraph 2 of this Article, dividends shall not be taxed in the Contracting State of which the company paying the dividends is a resident if the beneficial owner of the dividends is a resident of the other Contracting State and either:

(a) is a company that has owned, directly or indirectly, shares representing at least 50 per cent of the voting power of the company paying the dividends for the period of six months ending on the date on which entitlement to the dividends is determined; or

(b) is a pension fund or pension scheme, provided that such dividends are not derived from the carrying on of a business, directly or indirectly, by such pension fund or pension scheme.

Recommendation

Exemption of dividend income derived by Australian superannuation funds from tax in the foreign jurisdiction

Australia should consider the inclusion of equivalent clauses in future treaties or renegotiation of existing treaties, to exempt dividend income derived by Australian superannuation funds from tax in the foreign jurisdiction.

4. ‘Lump sum’ reference in Pension, Annuities and Similar Payment Articles

ASFA submits there are inconsistencies with the definition of ‘pensions, annuities and similar payments’ in tax treaties. In turn, these definitions do not always include ‘lump sum’ payments. The lack of ‘lump sum’ payments being included in the relevant article of treaties, creates unnecessary confusion for members of superannuation funds and, in turn, for superannuation funds as the withholding agents. The correct treatment is that the lump sum payments are subject to withholding tax at source (that is, in Australia). However, this is not clear in the tax treaties that Australia has entered into.

Below are examples of various differing approaches currently contained in 'pension, annuities and similar payment' articles in treaties:

- the UK and Singapore treaties with Australia include pensions and define annuities but are both silent on the treatment of lump sums
- the US-Australia treaty defines both pensions and annuities but is silent on the treatment of lump sums
- the NZ-Australia treaty does not refer to annuities at all but is clear as to the treatment of lump sums.

Recommendation

References to 'lump sum'

In negotiating tax treaties with other countries, and/or renegotiating or liaising with jurisdictions in respect of existing tax treaties, key outcomes should include:

- use of a consistent definition of 'pensions', including the key characteristics of periodic payments, made by reason of retirement or death, and for life or an ascertainable period of time; and
- in the relevant 'pensions, annuities or similar payments' article of each treaty, clarity as to the treatment of lump sum payments — in particular, that a lump sum arising in a Contracting State paid to a resident of the other Contracting State under a pension scheme, or in consequence of retirement, invalidity, disability or death, or by way of compensation for injury, is to be taxed in the first-mentioned State.

5. Comments specific to United States-Australia treaty

The US-Australia treaty does not address the US tax consequences of income accrued, other gains or accretions and contributions nor distributions from Australian superannuation funds to a US person. This impacts US persons working in Australia who are members of Australian superannuation funds, and also impacts Australians working in the US if they become relevantly connected in the US and continue to hold Australian superannuation accounts.

Under US tax law, Australian superannuation funds do not qualify as 'qualified retirement plans' (s401(a) of the Internal Revenue Code of 1986 (the Code)) and accordingly, Australian superannuation funds are not eligible for the tax concessions that are afforded to US retirement funds including the deferral of US taxes. Rather, the US tax treatment of Australian superannuation funds falls within s402(b) of the Code.

On this basis, there is confusion as to whether contributions that are made into an Australian superannuation fund by the employers of US persons are effectively treated as wage income of the US person and are included in the US person's US gross taxable income (section 83 of the Code).

Further, on this basis, investment income accrued within the US person's Australian superannuation account may also be taxable to that US person in the US. The US taxation of these accrued amounts may occur when that accrued income is paid by the Australian superannuation fund to the US person (section 72 of the Code).

However, US persons that are deemed to be "highly compensated employees" for US tax purposes may be subject to US tax on their accrued benefit in the Australian superannuation fund at the end of each year rather than at the time it is paid to the US person by the superannuation fund (section 402(b)(4) of the Code). Such US persons would therefore be taxed not only on employer contributions made to the Australian superannuation fund but also on the investment earnings accumulating in their Australian superannuation accounts on a year-by-year basis.

Australia's Treaty with the US does not address this issue. There is, however, precedent of the US having reached agreement with the UK (and also with Canada) to correct for this issue between their two countries, specifically Article 18 paragraph 5 of the US-UK Double Tax Treaty, extract as follows:

> *5. a) Where a citizen of the United States who is a resident of the United Kingdom exercises an employment in the United Kingdom the income from which is taxable in the United Kingdom and is borne by an employer who is a resident of the United Kingdom or by a permanent establishment situated in the United Kingdom, and the individual is a member or beneficiary of, or participant in, a pension scheme established in the United Kingdom,*
>
> *(i) contributions paid by or on behalf of that individual to the pension scheme during the period that he exercises the employment in the United Kingdom, and that are attributable to the employment, shall be deductible (or excludable) in computing his taxable income in the United States; and*
>
> *(ii) any benefits accrued under the pension scheme, or contributions made to the pension scheme by or on behalf of the individual's employer, during that period, and that are attributable to the employment, shall not be treated as part of the employee's taxable income in computing his taxable income in the United States.*

Recommendation

US-Australia tax treaty

A modification to the US-Australia treaty should be made — as has been afforded to the UK — so that:

- contributions paid by or on behalf of an individual to an Australian superannuation fund, attributable to employment, are deductible (or excludable) in computing the taxable income of the individual in the United States
- in turn, any benefits accrued under the superannuation fund, or contributions made to the superannuation fund by or on behalf of the individual's employer, that are attributable to the employment, are not included in the individual's taxable income in the US.

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File Name: 2016/06

1 April 2016

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Dear Sir/Madam

Re: OECD Public Discussion Draft – "Treaty Residence of Pension Funds"

The Association of Superannuation Funds of Australia (ASFA) is pleased to provide this submission in response to the above OECD Discussion Draft ("DD").

About ASFA

ASFA is a non-profit, non-political national organisation whose mission is to continuously improve the superannuation system so people can live in retirement with increasing prosperity. We focus on the issues that affect the entire superannuation system. Our membership, which includes corporate, public sector, industry and retail superannuation funds, plus self-managed superannuation funds and small APRA funds through its service provider membership, represent over 90 per cent of the 14 million Australians with superannuation.

ASFA notes that the primary term for "pension funds" in Australia is "superannuation fund" and these terms are used interchangeably throughout this submission.

ASFA also notes that all comments on the DD will be made publicly available by the OECD, and agrees to ASFA being publicly identified in this way.

ASFA has also provided a copy of this submission to representatives of the Treasury of the Commonwealth of Australia to inform Treasury's representations and ongoing discussions in respect of the proposed changes to Articles 3 and 4 of the OECD Model Tax Convention ("the Convention") and to the Commentary on these Articles ("the Commentary").

General comments

ASFA welcomes the OECD's moves to enable pension funds to access the benefit of tax treaties by treating them as a resident of the State in which they are constituted under the Convention.

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Australian superannuation or pension funds are some of the largest Australian investors in foreign jurisdictions. The present total funds under management ("FUM") of Australian superannuation funds is approximately AUD $2 trillion, and is anticipated to rise to more than AUD $9 trillion by 2030. A significant share of the existing FUM is invested outside Australia, and this share is anticipated to increase as the total size of the Australian superannuation sector increases.

Accordingly, greater clarity in the residency status of Australian superannuation funds would assist in removing or reducing taxation barriers caused by double taxation of income or capital gains derived by such funds, and thus would assist the entire Australian superannuation industry in its primary objective to advance the retirement outcomes for Australians.

The DD was framed in the context of potential changes to Articles 3 and 4 of the Convention and Commentary, to ensure that a pension fund is considered to be a resident of the State in which it is constituted for the purposes of tax treaties.

ASFA notes that, for many large Australian superannuation funds, this is a significant practical issue for Australia's present tax treaties. Australian superannuation funds have encountered practical issues in some jurisdictions in being treated as residents of Australia for the purposes of the treaty, and these impose costs in making detailed representations or collating substantial documentation in respect of funds' underlying members in those jurisdictions. Accordingly, by providing certainty in respect of the funds' residency status, the proposed changes have the potential to increase economic efficiency.

The DD notes that the proposed changes to Articles 3 and 4 of the Convention, and related Commentary, in respect of the definition of "recognised pension fund" will likely include the following elements:

- the definition will refer to entities or arrangements established in a State and constituted and operated exclusively or almost exclusively to administer or provide retirement or similar benefits to individuals
- the entities or arrangements to which the definition will apply will need to be treated as separate persons under the taxation laws of that State
- in order to cover only funds that the tax law recognises as pension funds, these entities will need to be regulated as pension funds by the State in which they are established
- the definition will also need to cover entities and arrangements that are constituted and operated exclusively or almost exclusively to invest funds for the benefit of entities or arrangements that will themselves qualify as "recognised pension funds"
- the definition will need to be accompanied by detailed Commentary that will explain some of these requirements, in particular the requirement that a pension fund "be regulated as a pension fund".

ASFA understands that, pursuant to the broader Action Plan on Base Erosion and Profit Shifting (BEPS), Australia may sign up to a "multilateral agreement" to streamline the implementation of the measures developed to address BEPS, in particular by modifying bilateral tax treaties. If so, this may result in changes to the Convention and Commentary being taken into account in determining residency for Australian pension funds in relation to the treaties with all of the other countries that sign up to this agreement. In this way, the proposed changes may have broader application, and not be limited only to Australia's new or renegotiated treaties.

Specific Responses to the Matters Raised in the DD

In respect of the specific matters raised in the DD, ASFA sets out its comments below.

a) ***As regards the phrase "that is treated as a separate person under the taxation laws of that State" included in the definition of "recognised pension fund" in proposed Art. 3(1) j):***
Does that phrase deal adequately with pension funds established in your State? If not, what other formulation would ensure that pension funds, the income of which is not otherwise attributed to another person for tax purposes, are treated as residents?

ASFA considers that this phrase deals adequately with all Australian superannuation funds.

b) ***As regards the phrase "that is constituted and operated exclusively to administer or provide retirement or similar benefits" included in subdivision i) of the definition of "recognised pension fund" in proposed Art. 3(1) j):***
Is the word "exclusively" too restrictive given the normal operations of a pension fund? If yes, please describe the operations that might not be covered, taking into account the fact that the subparagraph refers not only to "retirement benefits" but also to "similar benefits"?

In relation to this question, ASFA notes that the purpose for which an Australian superannuation fund may be maintained is expressly set out in section 62 of the primary Australian legislation governing superannuation funds, being the *Superannuation Industry (Supervision) Act 1993 (Commonwealth of Australia)*. This section is commonly known within Australia as the "sole purpose test".

Section 62 requires that a superannuation fund must be maintained solely for one or more of the purposes set out in subsection 62(1)(a) ("the core purposes"), or for one or more of the core purposes together with one or more of the purposes set out in subsection 62(1)(b) ("the ancillary purposes").

The core purposes include:

- the provision of benefits for each fund member on or after the member's retirement from any business, trade, profession, vocation, calling, occupation or employment in which the member was engaged

- the provision of benefits for each fund member on or after the member's attaining age 65

- the provision of benefits to the legal personal representative and/or the dependants of a fund member on or after the death of the member, provided that the death of the member occurred before he or she retired or attained age 65.

The ancillary purposes include:

- the provision of benefits for each member on or after termination of employment (which includes resignation, redundancy, etc.) from an employer who had at any time contributed to the fund in relation to the member

- the provision of benefits for each member on or after the member's temporary or permanent cessation of work on account of physical or mental ill-health

- the provision of benefits in respect of a deceased member, to the member's legal personal representative and/or to dependants of the member, where the member dies after retirement or after reaching age 65 (commonly referred to as "reversionary benefits")

- the provision of such benefits as the primary Australian prudential regulator of superannuation funds (the Australian Prudential Regulation Authority or APRA) approves in writing.

ASFA notes that paragraph 10.5 of the proposed Commentary on Article 3 in the DD cites payments made as a result of the death or invalidity of a person as an example of other "similar benefits".

In an Australian context, this example would appear to result in "retirement or similar benefits" including all of the above core and ancillary purposes.

However, ASFA submits that for clarification, the Commentary should expressly state that "retirement or similar benefits" includes:

1. Payments made by funds on or after the ordinary retirement date, notwithstanding that the person may continue in employment beyond that date. In Australia, a member has limited access to his or her entitlements after age 55 (or later "preservation age"), and unfettered access at age 65 (historically Australia's ordinary retirement date), notwithstanding that he or she may still be working at those dates.

2. Payments made by funds as a result of the temporary invalidity of a person - that is, that the reference in the Commentary to "invalidity" extends not just to permanent incapacity but also to temporary incapacity. In Australia, temporary incapacity benefits are able to be paid in the form of income payments replacing part or all of the salary or wages that would otherwise have been received by members.

3. Payments made by funds following the certification that a member is suffering from a terminal medical condition that is anticipated to result in death within 2 years. In Australia, a member has access to his or her entitlements following such a certification, notwithstanding that the member's illness may not yet have reached the point of invalidity.

4. Payments made by funds in rare circumstances following the termination of a member's particular employment. In Australia, most superannuation entitlements are subject to strict rules, such that access is not available until age 55 at the earliest. However, due to rules applying to some benefits that accrued prior to 1999, a portion of member's entitlements (known as "non-preserved benefits") may still be accessible upon termination of a member's particular employment prior to age 55.

5. Payments made by funds to temporary residents only, upon cessation of residence. In Australia, it is mandatory that the accrual of benefits in Australian pension funds for temporary residents of Australia be paid out to the members or to the Australian Government within 6 months of the cessation of residence by such members.

6. Payments made by funds in rare or special circumstances. In Australia, benefits may be paid outside the usual access restrictions to persons who satisfy the definition for being in "severe financial hardship", or who satisfy the conditions for APRA to allow payment on "compassionate grounds". Recipients of benefits prior to age 55 on the grounds of "severe financial hardship" are limited to payments of no more than AUD $10,000 in a 12 month period. APRA specifically determines the extent of benefits on "compassionate grounds" on a case by case basis, taking into account the reasons for the member's need for such access.

7. Payments made by funds below a de minimus amount. In Australia, benefits below AUD $200 may be paid outside the usual access restrictions to persons upon the termination of a member's particular employment.

Subject to the Commentary expressly dealing with each of the above circumstances, ASFA considers that the word "exclusively" is not too restrictive given the normal operations of Australian superannuation funds.

c) ***As regards the phrase "similar benefits" included in subdivision l) of the definition of "recognised pension fund" in proposed Art. 3(1) j):***
Are there examples of "benefits" that are typically granted by pension funds that would not be covered by the phrase "similar benefits"? If yes, please describe these benefits.

ASFA refers you to its comments in its response to question b) above.

As noted, Australia's superannuation legislation specifically restricts the purposes for which an Australian pension fund may be established and maintained. These restrictions set clear boundaries in respect of the circumstances in which an Australian pension fund can pay benefits to its members.

However, beyond these types of monetary benefits paid by funds, Australian superannuation funds may also provide other benefits to members.

These may include:

- incidental advantages that may accrue to members arising from an Australian pension fund's investments (for example, investment in a well-researched and commercially sound project that might incidentally create employment opportunities for the fund's members); or
- fund-sponsored member awareness, education and financial advice programs, targeted at fund specific issues such as benefit features (including insurance options, investment options).

In Australia, the extent of these other benefits is significantly curtailed. For example, whilst a fund may offer a financial planning service aimed only at a member's interest in the fund, APRA has stated that the provision by a fund of financial planning services aimed at broader non-superannuation savings and investment opportunities, products or services, such as investment or tax advice and health insurance would contravene the "sole purpose test". APRA notes that, in an Australian context:

- it would be inappropriate for the cost of such services to be borne by a fund, as the subject for such advice is not within the core or ancillary purposes for which a fund must be established and maintained; and
- funds wishing to make such broad services available to members would need to consider other means for funding the services.

ASFA submits that the Commentary should expressly note that the provision of incidental advantages arising from investments of the kind noted above, and financial planning services aimed only at a member's interest in the fund, would not result in a pension fund not being regarded as "constituted and operated exclusively or almost exclusively to administer or provide retirement or similar benefits to individuals".

d) ***As regards the phrase "that is constituted and operated exclusively to invest funds for the benefit of entities or arrangements" included in subdivision ii) of the definition of "recognised pension fund" in proposed Art. 3(1) j):***
Is the word "exclusively" too restrictive given the normal operations of an intermediary that invests on behalf of pension funds and, in particular, the possibility that these operations would include activities that are not related to the investment of funds and the possibility that non-resident pension funds would be investing through such an intermediary? If yes, please describe the operations that might not be covered?

ASFA notes the comments in paragraph 10.8 of the proposed Commentary on Article 3 in the DD that pension funds often invest together with other pension funds pooling their assets in certain arrangements or entities and may, for various commercial, legal or regulatory reasons, invest via wholly owned entities or arrangements that are residents of the same State. ASFA concurs with these comments, and supports the following sentence in the same paragraph in the DD that, since such arrangements and entities act only as intermediaries for the investment of funds used to provide retirement benefits to individuals, it is appropriate to treat them like the pension funds that invest through them.

In Australia, the primary entities presently used to pool the assets of superannuation funds are:

1. Life insurance companies, which as corporations established and maintained in Australia would already be treated as Australian residents for treaty purposes.

2. Pooled superannuation trusts ("PSTs"), which are taxed in Australia in the same manner as Australian superannuation funds. The beneficial owners of the units in a PST are restricted by Australian law to Australian superannuation funds and/or life insurance companies in respect of policy holders who are themselves Australian superannuation funds.

3. Unit trusts ("UTs"), which are flow through entities in Australia, such that any Australian tax is paid by the beneficial owners of the units in the UT. The beneficial owners of the units in a UT are not restricted to Australian superannuation funds, and thus may also include individuals, corporations, and non-Australian pension funds.

As noted, it is not necessary that life insurance companies in Australia be covered by proposed Article 3(1) j), as the residency of corporations is already addressed in the Model Convention.

ASFA considers that the word "exclusively" is not too restrictive in an Australian context given the normal operations of an Australian PST or UT. In Australia, these entities are by their very nature restricted to activities relating to the investment of funds, and any other operations would be wholly incidental and subordinate to these investment functions.

However, ASFA submits that the Commentary should clarify two aspects.

1. *Passive versus active investment*

   ASFA notes that the nature of the investments for some pension funds may involve the pension fund taking an active role, rather than just being the passive recipient of investment income. For example, a fund (or the wholly owned or pooled investment vehicle) may undertake property development rather than just the holding of property for rent.

   In this light, ASFA submits that the Commentary should note that the references to investment are not restricted to passive investment only.

2. *Entities not exclusively owned by pension funds from the particular State*

   As noted above, it is possible for an Australian UT to have unit holders that are not exclusively Australian pension funds.

   For some UTs, there will be no such possibility, for example:

   - a UT that is established and maintained exclusively:
     - as the wholly owned investment vehicle for a single Australian superannuation fund, or

    - for the pooling of investments of Australian superannuation funds only; or

- a "closed fund" UT that is established with its only unit holders being Australian superannuation funds, and which has no capacity for new unit holders to be admitted or for the transfer of units to other persons

  For these UTs, ASFA considers that the word "exclusively" is not too restrictive in an Australian context, and that the Australian Taxation authority (the Australian Taxation Office ("ATO")) should readily be able to provide a Certificate of Residency or similar support to such entities to provide to jurisdictions with which Australia has treaties based on such words.

ASFA submits that the Commentary should note that, for entities not exclusively owned by pension funds from the particular State, reference would need to be had to the existing guidance in the 2010 OECD Report *The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles* (CIVs), and to the outcomes of the separate consultation and Public Discussion Draft of 24 March 2016 in respect of the Treaty Entitlement of Non-CIV Funds.

In an Australian context, ASFA notes that it is likely that for any UT that is not exclusively owned by Australian pension funds to be treated as an Australian resident, it would have to prove that its existing unit holders do not include non-Australian residents, and provide such other evidence as the ATO may require in order to obtain a Certificate of Residency.

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Should you have any questions on any of the matters raised in this submission please contact Julia Stannard via email jstannard@superannuation.asn.au.

Yours sincerely

Glen McCrea
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