

15 November 2010

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

Attention: Raphael Cicchini

Dear Mr Cicchini

**IMPLEMENTATION OF A NEW TAX SYSTEM FOR MANAGED INVESTMENT TRUSTS
DISCUSSION PAPER**

We welcome the opportunity to make a submission to Treasury on the discussion paper for the implementation of a new tax system for Managed Investment Trusts (MIT) (“the Discussion Paper”).

Moore Stephens commends the Government on their initiative to improve the international competitiveness of the Australian funds management industry by providing fund managers with further certainty in the introduction of the new MIT tax system. However, considering the short period for consultation we have only provided our broad comments.

1. Submission

This submission follows up our submissions to Treasury dated 22 December 2009 and 10 July 2009 and the Board of Taxation dated 2 December 2008.

1.1 One MIT definition

The rules about trusts treated as MIT’s for the purposes of the capital account election (Division 275) should be incorporated in the concept of a MIT that applies generally to the treatment of MIT’s for income tax. This will minimise complexity for tax payers – one of the stated objectives of Australia’s Future Tax System Review Panel.

1.2 Attribution method of taxation

Specific rules which list those documents that form part of a MIT’s constituent documents should be adopted to provide certainty for trustees of managed funds.

A potential compliance issue of the requirement under the attribution method that tax losses in respect of one class of unit holders cannot be used to reduce the tax income of another class of unit holders is the application of the loss recoupment tests to each class of unit holders, as opposed to the trust as a whole.

Modifications to the proposed attribution rules should not be required for trustees of trusts where units may be traded on a more regular basis. This is to ensure consistency for all MIT’s.

1.3 Unders and overs – carry forward arrangements

There should also be statutory rules for overs and unders relating to tax offsets and the appropriate *de minimus* threshold should be the same as the threshold for overs and unders in relation to the tax income of a trust. This is to ensure consistency in the legislation and minimise compliance costs for trustees of managed funds.

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We suggest that where an under or over does not exceed the *de minimus* threshold, the suitable operative mechanisms to ensure that the trustee does not need to issue revised distribution statements and that assessments made in accordance with distribution statements do not need to be amended are as follows:

- There should be no change to the amount of the tax income of the MIT;
- an under should not be assessed to the trustee; and
- the under or over should be carried forward into the MIT's tax income calculation for the next income year following identification of the error and affect amounts assessable to unit holders in that year.¹

This is the current industry practice and incorporating this into the proposed legislation will minimise compliance costs for trustees of managed funds transitioning into this new regime.

In applying the carry forward of an under or over not exceeding the *de minimus* amount in a later income year, constituent amounts (e.g. capital gains, franking credits) should be applied specifically against an amount of the same type and this should be for all categories of income. This is the current practice for our clients and reflecting this in the proposed legislation will minimise compliance costs for trustees of managed funds transitioning into this new regime.

The specified period that should be allowed for the trustee to reissue distribution statements to beneficiaries after becoming aware that there is an under exceeding the *de minimus* amount is three (3) months after the end of the financial year (i.e. 30 September). This will provide individual investors with sufficient time to lodge their income tax returns by the earliest due date of 31 October.

1.4 Cost base adjustments

There will be an increase in compliance costs associated with requiring a MIT to trace cost base movements on each event, but it should not be significant.

The requirement for MIT's to notify unit holders of cost base adjustments should be on an annual basis through an annual statement. However, cost base adjustments should be made for each attribution and distribution. Accordingly, the annual statement should inform beneficiaries of the cost base adjustments for all distributions paid during the income year.

No modifications to the proposals are warranted for MIT's that are Exchange Traded Funds as their distribution frequency is similar to other managed funds. This is to ensure consistency for all MIT's.

1.5 Character and source retention

The proposed approach for character and source retention is workable in practice.

1.6 Repealing corporate unit trust rules and including an arm's length rule in the public trading trust rules

We support the repeal of the corporate unit trust rules in Division 6B of Part III of the Income Tax Assessment Act 1936.

We believe that the proposed arm's length rule for the public trading trust regime in Division 6C of Part III of the *Income Tax Assessment Act 1936* should only be implemented if Recommendation 9 of the Board of Taxation's report to the Assistant Treasurer is adopted. That is, we see no need for the added compliance complexity of an arm's length rule unless:

- Division 6C is amended to allow an MIT to own directly, or through a chain of entities, 100% of the ownership interests in a single taxable subsidiary company; and

¹ Paragraph 74 of the Discussion Paper

- The amendment described above is followed by a post-implementation review by the Board of Taxation which considers whether it is appropriate to allow MITs to have any number of taxable wholly-owned subsidiaries engaging in active business.

We highlight that the stakeholders that suggested the introduction of an arm's length rule envisaged supporting its introduction as a trade-off for a very specific concession. This concession would allow MITs to continue to be taxed as trusts where they have subsidiaries that conduct ineligible activities, so long as those subsidiaries are taxed as companies. This concession was thought to strike a correct balance between increasing the international competitiveness of Australian MITs and avoiding an excessive erosion of the corporate tax base. The arm's length rule would protect the corporate tax base by ensuring that an MIT could not shift profits out of its Australian resident corporate taxed subsidiaries.

1.7 Other issues

The trustees of MIT's should not be required to notify unit holders of the amount of unders and overs identified and to be carried forward. They do not notify unit holders currently and we don't believe that unit holders will be concerned with relatively immaterial differences.

MIT's would need time before the commencement of the new attribution rules to amend trust deeds. A reasonable amount of time for this is three (3) months.

2. Moore Stephens - sector experience

We recognise that there is huge diversity in the investment specialties of MIT's. These include Australian and foreign equities, property and private equity.

Moore Stephens member firms² provide taxation services to more than 100 managed funds, fund managers and LIC's primarily investing in Australian equities and 10 property fund managers who manage over 60 listed and unlisted Real Estate Investment Trusts (REIT's) and their subsidiaries that invest in property located in Australia and over 10 foreign countries. Moore Stephens member firms have been advising the financial services sector in relation to financial reporting, taxation, corporate governance and general advice for over 10 years. Our involvement with these entities encompasses a diverse range of investment activities and structures.

Thank you for considering our submission. If you have any questions regarding the above, please do not hesitate to contact me.

Yours faithfully
MOORE STEPHENS



Allan Mortel
Chairman
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² Moore Stephens is a network of independent firms