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International Tax Framework Unit
International Tax and Treaties
Division
The Treasury
Langton Crescent
PARKES ACT 2600

Attention: Lisa Clifton

Dear Treasury

Managed Investment Trust (MIT): Submission on the Exposure Draft Legislation Tax Laws Amendment (2010 Measures No. 3) Bill 2010

The Taxation Institute of Australia ("**Taxation Institute**") is pleased to provide comments on the exposure draft legislation in the form of the *Tax Laws Amendment (2010 Measures No. 3) Bill 2010* ("**Exposure Draft**") which was released for public comment on 16 April 2010.

However, the Taxation Institute is disappointed about the timeframe allocated for this consultation. One week is not sufficient to allow genuine consultation. Further, one week does not provide sufficient time for detailed consideration and debate of all relevant issues arising under the Exposure Draft.

1. Summary

The Taxation Institute welcomes the Assistant Treasurer's announcement[1] ("**Announcement**") to more closely align the definition of a "managed investment trust" ("**MIT**") under section 12-400 of Schedule 1 of the *Taxation Administration Act 1953* ("**TAA**") with the definition of a MIT in the *Tax Laws Amendment (2010 Measures No. 1) Bill 2010* ("**No.1 Bill**").

The Taxation Institute's recommendations in relation to the Exposure Draft are as follows:

- **Recommendation 1:** The changes introduced by the Exposure Draft should not have retrospective effect.
- **Recommendation 2:** The Exposure Draft should be amended to ensure that a trust with only one member can qualify as a MIT.

[1] See Media Release No. 020 of 10 February 2010.

- **Recommendation 3:** The "operated AND managed" requirement in proposed section 12-400(1)(item 2) of the Exposure Draft should be removed.

- **Recommendation 4:** The Exposure Draft should clarify the position in relation to unregistered managed investment schemes ("**MISs**") which are not engaged in trading.

Each of the above recommendations is discussed in further detail below.

2. Recommendation 1: The Exposure Draft should not have retrospective effect

Any changes to the meaning of a MIT made by the Exposure Draft should not apply to MITs created before the Exposure Draft receives Royal Assent. Grandfathering provisions should be introduced in relation to the proposed changes to the meaning of a MIT in section 12-400 of Schedule 1 in the Exposure Draft (including those changes that relate to carrying on a trading business in proposed section 12-400(6) and changes relating to small groups in proposed section 12-400(7)).

This is necessary to create certainty for foreign investors who have already established a trust that currently qualifies as a MIT.

3. Recommendation 2: Ensure that a trust with only member can qualify as a MIT

Clarification is needed in relation to the operation of the definition of a MIT where there is only one member. This was part of the Assistant Treasurer's Announcement.

The proposed amendment to subsection 12-400(1) in Schedule (paragraph (c) of item 3 of the table) on the Exposure Draft is intended to permit a trust with one member to qualify as a MIT.

However, a trust with one member will not qualify as a MIS under section 9 of the *Corporations Act 2001* ("**Corporations Act**").

Bill No.3 should be amended to ensure that a trust with one member will be treated as a MIS for the purposes of the definition of a MIT or otherwise come within the definition of an MIT.

4. Recommendation 3: Remove the "operated AND managed" requirement in proposed section 12-400(1)(item 2)

Proposed section 12-400(1)(item 2) of the Exposure Draft provides that a trust that is a MIS must be operated **and** managed by a financial services licensee whose licence covers operating such a MIS.

This requirement in the Exposure Draft does not mirror the requirement in the No.1 Bill. The No.1 Bill provides in section 275-5(1)(b) that:

> *"the trust is operated **or** managed by*
>
> *(i) a financial services licensee …."* [Emphasis added.]

The Exposure Draft therefore does not result in closer alignment of the definition of a MIT in the No.1 Bill; rather the Exposure Draft introduces a new requirement that a trust be both operated and managed by a financial services licensee.

It is not clear from a policy perspective:

(a) why a trust should be both operated and managed by a financial services licensee;

(b) whether proposed section 12-400(1)(item 2) requires a trust to be operated and managed by the same financial services licensee or whether those functions can be carried out by different entities;

(c) if the operation and management of the trust can be carried out by different entities:

(i) why are both the operator and manager required to hold a licence that covers operating a MIS;

(ii) what happens if both the trustee and the manager carry out management activities - if the trustee's licence covers operating a MIS, is it necessary for the manager to also hold such a licence;

(iii) if there are numerous managers, must each manager have the required licence; and

(iv) what happens if the manager is exempt from holding the required licence (and what is the policy reason for requiring a licence when such a licence is not required under the Corporations Act?);

(d) what is intended by, and what is the scope of, the "management" requirement; or

(e) to what extent the operation and management of the trust must be in Australia[2].

These matters should be clarified. Further, there needs to be a clear explanation of what is meant by the words "and managed" in relation to registered schemes. The Taxation Institute submits that the operation and management requirements should be expressed as alternative conditions, consistently with the No.1 Bill.

5. Recommendation 4: Clarify the position in relation to unregistered MISs

There has been some confusion regarding whether a trust must actually be registered to be a MIT. This confusion has arisen because:

(a) Section 12-400 of Schedule 1 of the TAA does not expressly require a MIT to be registered under the Corporations Act.

[2] Section 12-400(1)(item 1) contains the required residency nexus for a trust. The trustee either must be resident in Australia, **or** the central management and control of the trust must be in Australia.

(b) The Explanatory Memorandum to the legislation which enacted section 12-400 of Schedule 1 provides (at paragraph 1.37) that:

> *"The tracing rule recognises that a managed investment scheme established by a wholesale trust would otherwise fail to satisfy the test of being widely held, even if interests in the wholesale trust were held by entities with more than 50 members."*

A wholesale trust would usually not be registered, because the trust would not be required to be registered under the Corporations Act.

(c) However, ATO Interpretive Decision ATO ID 2009/150 provides that an unregistered MIS cannot satisfy the definition of a MIT in section 12-400(1) of Schedule 1 of the TAA because an unregistered MIS is not operated by a financial services licensee whose licence covers the operation of such a MIS.

(d) Similarly where an unregistered MIS is managed and/or operated by an entity that does not hold a financial services licence, the MIS can not satisfy the definition of an MIT. Where the trust is not engaged in trading, there seems to be no policy reason why the trust should not have the benefit of being treated as an MIT.

The position should be clarified in Bill No.3. Any such clarification should be subject to our comments on laws having retrospective effect in part 2 above.

The Taxation Institute submits that, provided that the relevant licence is held by the trustee, the trust need not actually register as a MIS. There is no policy reason why registration should be required where all of the other conditions are met.

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If you require any further information or assistance in respect of our submission, please contact David Williams on 02 9958 3 or the Taxation Institute's Tax Counsel, Angie Ananda, on 02 8223 0011.

Yours sincerely

David Williams
President