THE SENATE

BILLS


Second Reading

SPEECH

Wednesday, 4 May 2016

BY AUTHORITY OF THE SENATE
Senator CANAVAN (Queensland—Minister for Northern Australia) (10:01): I move:

That the bills be now read a second time.

I seek leave to have the second reading speeches incorporated in Hansard.

Leave granted.

The speeches read as follows—

TAX LAWS AMENDMENT (NEW TAX SYSTEM FOR MANAGED INVESTMENT TRUSTS) BILL 2015

This Bill is part of a broader package of Bills that amend various taxation laws to introduce a new system for taxing managed investment trusts (MITs).

The new rules will modernise the tax rules applying to eligible MITs, increase certainty for MITs and their investors, and reduce complexity. It will reduce compliance costs by $30 million per year for MITs and their investors. These reforms will enhance the competitiveness of Australia's funds management industry.

Our managed funds industry is one of the largest and most sophisticated in the world. As of 30 June 2015, Australia had $2.6 trillion in funds under management, larger than Australia's gross domestic product and the capitalisation of the Australian Stock Exchange. It is one of the largest pools of managed funds in the world, and contributes jobs to the broader financial and insurance services industry, which employs over 400,000 people in Australia. We need to ensure that this industry continues to support Australian jobs, and remains efficient and internationally competitive.

Managed investment trusts are used by many Australians. Most of us are investors in MITs, either directly or indirectly through our superannuation funds. MITs are used to invest in a diverse range of assets, including shares, property, bonds and cash.

The current taxation arrangements applying to trusts are complex and uncertain. This is unacceptable for an industry so significant to the economy and the financial security of Australians. This Bill will ensure that the funds management industry is able to operate more effectively through trust structures.

This new tax system will also provide an opportunity for Australia’s managed funds industry to grow by exporting more of its expertise and attracting additional international investment. This will in turn increase growth and jobs.

The Government’s new tax rules for eligible MITs follows recommendations made by the Board of Taxation in its Report on the Review of the Tax Arrangements Applying to Managed Investment Trusts.

In its review, the Board found that current tax arrangements applying to trusts create undue complexity and uncertainty for MITs. Specifically, trust tax rules have not kept pace with the growing use of trusts as collective investment vehicles. The Board recommended the creation of new tax rules for eligible MITs.

The new tax system has been actively sought by the funds management industry. Key stakeholders have been extensively consulted during the development of the new tax system.

The new rules will apply from 1 July 2016. However, trustees can choose to opt in earlier and apply the rules for income years starting on or after 1 July 2015.

The new tax system will apply where the members of the trust have clearly defined interests in relation to income and capital of the trust and the trustee of the MIT makes a choice to apply the new rules.
Trusts that are not eligible or choose not to apply the new tax system will continue to apply the general trust tax rules.

The Bill will provide for taxation at the investor level, rather than at the entity level. Investors will generally be taxed on amounts as if they had derived the income directly.

Members will be taxed only on amounts 'attributed' to them. This amount is determined by the trustee according to the member's interest as set out in the constituent documents of the trust. The tax characteristics applying to that income will flow through to members.

The introduction of the attribution model will provide greater certainty for trustees and members, by more closely aligning the commercial and tax consequences of activities of a managed investment trust.

Under the new rules, trustees will continue to provide statements to their members shortly after the end of each income year to assist members to complete their tax returns. However, trustees may not have final information from entities that they invest in by the time they have to report to members. This means they often need to make estimates in the statements issued to members and then make adjustments at a later point in time when more information is available.

This can be administratively onerous. Because of this these Bills will give the trustee a choice to reconcile the variance in the income year it is discovered, or to reissue statements to members for the income year to which the variance relates. If the trustee reconciles the variance in the discovery year, members will not have to seek amendments to their income tax assessments. This will reduce compliance costs for MITs and their members, as well as administrative costs for the ATO. This approach is consistent with current industry practice. Associated integrity rules will encourage MITs to bring income to account in a timely way.

These Bills also introduce a new rule so that multi-class MITs will be able to elect to treat each class as a separate trust for the purposes of the new MITs tax system. The effect is that gains and losses within a class will be quarantined to those members. Currently, gains and losses relating to one class can affect another class of interests within the same trust. This amendment means that fund managers will be able to offer a range of different investment options through a single trust, rather than incurring higher costs from establishing multiple trusts to achieve the same outcome.

These Bills also remove the incidence of double tax for members of attribution MITs that currently arises under the capital gains tax rules. Where amounts distributed to members differ to the taxable income of the MIT, members will now be able to adjust the cost base of their investments so that they are not taxed twice. The current law required reductions in cost base where amount received by the member exceeds the taxable component of the distribution. However, there is no corresponding upwards adjustment to the cost base if the amount received is less than the taxable component of the distribution. The amendments will now allow upwards adjustments to the cost base in certain situations.

The Government will also introduce transitional provisions and consequential amendments as part of this package of Bills relating to the new tax system for MITs. This includes consequential amendments to ensure the MIT withholding tax rules apply appropriately under the new attribution model of taxation.

In addition, this package contains an arm's length rule that was recommended by the Board of Taxation. This rule will discourage MITs from shifting profits from an active business of a related party to the attribution MIT. The Commissioner of Taxation will be given powers to make a determination where a MIT has derived non-arm's length income. The trustee of a MIT will be liable to pay tax at the corporate rate on this income and other administrative penalties may apply. This will protect the integrity of the corporate tax base.

The 20 per cent tracing rule applying to certain unit trusts will also be amended so that superannuation funds and certain other exempt entities will be excluded. This will reduce compliance costs and allow trusts to avoid being taxed as a company simply because certain entities, such as superannuation funds, own more than 20 per cent interest in the trust.

Further, rules that tax corporate unit trusts as companies will be repealed. These rules were introduced when Australia had a classical tax system to discourage companies from restructuring as trusts. Companies had an incentive to restructure as shareholders faced the prospect of double taxation, due to the lack of imputation.
Since the introduction of imputation, the integrity rules for corporate unit trusts are considered to be no longer necessary and will be repealed.

Together, the measures contained in this package of Bills will reduce complexity, increase certainty and minimise compliance costs.

In conclusion, this package of Bills recognises the commercial needs of the industry and the growing use of trusts as commercial investment vehicles. Greater certainty will benefit investors and the managed fund industry.

It will improve the attractiveness of Australian MITs to international investors. It will assist our managed funds industry to develop and export more of their services. This should increase growth and jobs.

The new tax system for MITs has been actively sought by the managed investment funds industry. The Government has listened to this. The Government has undertaken extensive consultation with industry representatives and other key stakeholders in the development of this new MITs tax system.

The new rules will ensure that the managed funds industry is able to continue to operate through trust structures having regard to the commercial needs of industry, the needs of investors, and the need to ensure appropriate integrity, and minimise compliance and administrative costs.

As a result, the Government is confident that these new amendments will modernise the tax law applying to MITs. The measures contained in these Bills are vital to ensuring that Australians have the best opportunity to grow their income. The measures will also enhance Australia’s managed funds industry and promote the greater export of Australia’s funds management expertise.

Full details of the new tax system for MITs are contained in the explanatory memorandum.

INCOME TAX RATES AMENDMENT (MANAGED INVESTMENT TRUSTS) BILL 2015

The Income Tax Rates Amendment (Managed Investment Trusts) Bill 2015 forms part of a package of Bills to introduce a new system for taxing managed investment trusts (MITs).

This Bill specifies the rate of tax payable by trustees of attribution MITs in some circumstances. Under the new tax system, investors are generally taxed on amounts attributed to them by the trustee of a MIT, as if they had invested directly. In limited circumstances, tax may occur at the trustee level instead of at the investor level to ensure that correct tax outcomes occur. This primarily occurs if the trustee does not attribute all income to members. In this case, the trustee is taxed on the unattributed income, to ensure that this income does not escape taxation. The unattributed income is generally taxed in the hands of the trustee at the highest individual marginal tax rate, plus Medicare Levy.

Further details of the Bill and the new tax system applying to MITs are set out in the explanatory memorandum for the Tax Laws Amendment (New Tax System for Managed Investment Trusts) Bill 2015.

MEDICARE LEVY AMENDMENT (ATTRIBUTION MANAGED INVESTMENT TRUSTS) BILL 2015

The Medicare Levy Amendment (Attribution Managed Investment Trusts) Bill 2015 forms part of a package of Bills to introduce a new system for taxing managed investment trusts (MITs).

This Bill amends the Medicare Levy Act 1986 to impose the two per cent Medicare Levy on trustees of attribution MITs in some circumstances. Under the new tax system, tax is generally applied at the investor level. However, tax may be applied at the trustee level to ensure that correct tax outcomes occur. This primarily occurs if the trustee does not attribute all income to members. Where this is the case, the trustee will be taxed on the unattributed income at the highest individual marginal tax rate plus the Medicare Levy in certain circumstances. This operates to ensure that income does not escape taxation.

Further details of the Bill and the new tax system applying to MITs are set out in the explanatory memorandum for the Tax Laws Amendment (New Tax System for Managed Investment Trusts) Bill 2015.

INCOME TAX (ATTRIBUTION MANAGED INVESTMENT TRUSTS—OFFSETS) BILL 2015
The Income Tax Rates Amendment (Attribution Managed Investment Trusts#Offsets) Bill 2015 forms part of a package of bills to introduce a new system for taxing managed investment trusts (MITs).

This bill imposes income tax on trustees of attribution MITs where they attribute excess tax offsets to members in some circumstances. This can happen if the trustee overestimates the amount of offsets it has available to attribute to members in an income year. This means that members are able to reduce their tax liability more than they otherwise would, had they not been attributed excess offsets.

Tax will be payable by trustees of attribution MITs on the amount of the excess tax offsets at a rate of 100 per cent. This has the effect of clawing back excess tax offsets and neutralising the impact on tax revenue. This is consistent with outcomes that arise when a company passes out excess franking credits.

Further details of the bill and the new tax system applying to MITs are set out in the explanatory memorandum for the Tax Laws Amendment (New Tax System for Managed Investment Trusts) Bill 2015.