FINANCIAL SERVICES COUNCIL

Corporate Collective Investment Vehicle Framework and Other Measures Bill 2021

FSC Submission to Senate Economics Committee

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1. About the Financial Services Council

The FSC is a peak body which sets mandatory Standards and develops policy for more than 100 member companies in one of Australia's largest industry sectors, financial services.

Our Full Members represent Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advice licensees and licensed trustee companies. Our Supporting Members represent the professional services firms such as ICT, consulting, accounting, legal, recruitment, actuarial and research houses.

The financial services industry is responsible for investing $3 trillion on behalf of more than 15.6 million Australians. The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Securities Exchange, and is the fourth largest pool of managed funds in the world.

2. General comments

The FSC welcomes the opportunity to provide a submission on the Corporate Collective Investment Vehicle Framework and Other Measures Bill 2021 (**The Bill**).

The FSC's comments relate to two components of the Bill:

- The provisions relating to the Corporate Collective Investment Vehicle (**CCIV**) – Schedules 1 to 5 of the Bill.
- The provisions relating to the Retirement Income Covenant (**The Covenant**) – Schedule 9 of the Bill.

The FSC is a strong supporter of both of these components of the Bill and we support the passage of the Bill.

In relation to the CCIV, the Bill will provide a significant improvement in the range of investment vehicles that can be offered to both Australian and foreign investors.

In relation to the Covenant, this component of the Bill will ensure superannuation trustees are appropriately considering the retirement income needs of their members. The Covenant will require funds to have an increased focus on retirement of members, and should improve retirement outcomes for Australians.

Further comments on the importance of these two reforms are in Section 4 of this submission (Importance of Reforms in the Bill).

The FSC submits that Parliament should pass the Bill as soon as practicable, particularly given both the CCIV and the Covenant are set to start on 1 July 2022, there are a limited number of Parliamentary sitting days scheduled for the first half of 2022, and there is a likelihood that these days will be further curtailed by the election required in 2022.

Given these time pressures, the FSC and members consider it is important to provide certainty to the industry.

3. Specific comments on CCIV

3.1. Transitional arrangements

A key aspect to the success of the CCIV regime is the introduction of transitional relief to allow existing funds to convert into CCIVs. This relief will allow Australian fund managers to rationalise fund offerings through mergers and other structural changes without investors facing additional costs particularly relating to tax, stamp duty and investor meetings. A rationalisation of existing structures helps to remove unnecessary costs associated with maintaining outdated products and will likely help bring down the price of managed funds for consumers, and in the domestic market particularly.

With this short timeframe between announcement and implementation, it seems it was not possible to include transitional provisions in this draft, but we strongly support this and understand that current plans are for the government to introduce further legislation to include appropriate forms of transitional relief.

3.2. Additional improvements

We consider that there are a few improvements which should be considered at the same time as the further transitional legislation which would improve the operation of the new regime, increase its attractiveness, and ultimately ensure its long-term success. The FSC considers these issues should not hold up the passage of the Bill before the Committee.

The FSC wishes to draw attention to two specific issues discussed in more detail below. If these issues are addressed, this could improve the take up of the CCIV regime and its ultimate success. We consider these changes could be introduced very simply and should not involve a concern in relation to the fiscal integrity of the new regime.

Without these changes some fund managers may be less likely to take advantage of the new regime. However, even without these changes we believe it is appropriate to enact the current legislation as soon as possible.

3.3. Taxation of subfunds that fail widely held conditions

There are specific provisions in the CCIV sections of the Bill for the taxation of a CCIV sub fund that fails to satisfy the widely held conditions. The policy aim of these provisions is to produce an equivalent tax outcome to the current trust regime.

In the case of a managed investment trust (**MIT**), the trust deed will determine the income to which relevant beneficiaries must be presently entitled. By contrast, the CCIV legislation introduces a requirement that the amount to which beneficiaries must be presently entitled is based on accounting profits. This is different from the way managed funds normally operate.

The reliance on accounting profits will introduce issues for CCIV members. In some cases, it could result in extra tax being imposed on the subfund. It may also require significant system changes.

We believe that a simple solution to the problem is to remove reliance on a concept of accounting profits and rely on the definition of trust income as contained in the deed.

3.4. Tax rules relying on concepts of dividend

The tax rules for CCIVs do not apply based on entitlement to distributions, but instead rely on the tax definition of a "dividend". This approach introduces the detailed provisions for corporate distributions into CCIVs. The use of this expression will add complexity to the administration of a CCIV and in in some instances could prevent distributions to investors.

It may be challenging for the ATO to administer the legislation in a way which could ameliorate the impact of these issues.

We therefore submit that the reliance on dividend should be replaced by reliance on entitlement.

4. Importance of Reforms in the Bill

4.1. Corporate Collective Investment Vehicle

Collective Investment Vehicles (**CIVs**) are structures that are used around the world, and take many different forms depending on the legal structures available in each country. In general, CIVs allow investors to pool their money together to achieve economies of scale, diversification of risk, segregation of the assets, easy access to high quality investment decisions, and access to investment opportunities that individual investors alone could not otherwise enjoy.

Up till now, Australia has been limited in the type and number of CIVs with flowthrough tax treatment. Currently, managed investment trusts (**MITs**) are the only flowthrough investment vehicles available to Australian fund managers to manage collective investment pools.[1] However, Australian MIT structures are not well understood by foreign investors – instead corporate structures (like the proposed CCIV) are much better known in many other countries.

While some Asian nations utilise investment structures that are also called unit trusts, investor rights and obligations under these vehicles are usually codified, rather than being determined by case law. Further, some Asian nations operate under a civil code legal

[1] Listed Investment Companies or LICs are also used in Australia as collective investment vehicles but LICs do not have flowthrough tax treatment.

system that do not have similar structures. Even for those Asian nations that operate under a common law system, the codification of their investment vehicle law makes it easier to explain how investors will be treated and provides greater certainty about legal rights and obligations. Outside Asia, corporate investment structures are more commonplace. Australia does not have a comparable corporate investment vehicle.

In response to these concerns, the 2009 Johnson Review, *Australia as a Financial Centre — building on our strengths* recommended a CCIV regime be developed so that Australia could expand as a fund formation centre. When a fund is domiciled in Australia there are flow on benefits generated due to the increased economic activity from associated support services that are usually located where the fund is domiciled. These can include legal, accounting, fund administration and in some cases, custodial and or investment management activities.

The CCIV sought by industry, and contained in the Bill currently before Parliament, is a new kind of entity which does not currently exist in Australia's regulatory regime. It is a collective investment vehicle subject to the same tax treatment as a MIT but with some of the features of a company.

Like a MIT, the CCIV provisions in the Bill offer tax flow-through treatment so that the end investor is taxed at their marginal tax rate. For foreign investors, withholding tax is taken from distribution payments and remitted to the ATO by the CCIV operator.

While this concept is foreign to Australia's existing regime, it is quite commonplace overseas. The United Kingdom and Luxembourg both have well-established precedents for how such a vehicle can operate and be regulated, for example the Open Ended Investment Company (**OEIC**) and the Société d'Investissement à Capital Variable (**SICAV**), respectively. In addition, both Hong Kong and Singapore have recently introduced similar vehicles: the Open-Ended Fund (**OEF**) in Hong Kong, which was recently enhanced; and the Singapore Variable Capital Company (**SVCC**). Compared against these other jurisdictions, the lack of an Australian corporate investment vehicle is a clear gap.

Australia's new CCIV should increase the ability for local fund managers to compete globally. As a result, the CCIV should help increase exports of Australian investment products, as foreign investors will have Australian investment products that are more familiar and more internationally acceptable.

We welcome the many improvements to the CCIV regime that have occurred during comprehensive consultation with FSC and our members – particularly the removal of the requirement to have a depositary, and closer alignment of the CCIV tax regime with the current tax regime for Attribution Managed Investment Trusts (**AMITs**).

As noted earlier we consider the CCIV regime could benefit from improvements, which will add to the potential benefits of the CCIV over time, but we consider it is preferable to have the legislation in place soon rather than risk a major delay by calling for amendments at this stage.

The FSC strongly supports these issues being addressed in future development of the CCIV.

4.2. Retirement Income Covenant

The FSC is strongly supportive of a principles-based Retirement Incomes Covenant, which ensures superannuation trustees are appropriately considering the retirement income needs of their members.

The FSC is supportive of the proposed structure and content of the Covenant. It clearly builds on the findings of the Retirement Income Review to provide clear direction for trustee thinking on retirement issues.

We consider the requirement for funds to develop, implement and regularly review a Retirement Income Strategy for members is an appropriate addition to the existing legislated covenants. The three areas to be considered by trustees (income, risk, and access to savings) are also appropriate to reflect the key considerations when determining the best approach to retirement income for a fund members.

The FSC looks forward to working with Government and agencies (particularly APRA) on the detailed implementation issues relating to the Covenant.[2] We are particularly looking for an approach from regulators that recognises the limited time available before the start date of the covenant, and adopts a flexible and reasonable approach to regulator expectations and enforcement.

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[2] Some of the implementation issues for the Covenant have been raised in previous FSC submissions, including the FSC submission on the Covenant position paper and the FSC submission on the Exposure Draft of the Covenant legislation: https://fsc.org.au/resources/2304-fsc-submission-retirement-income-covenant-exposure-draft-legislation/file