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Ms Julie Owens MP
Chair House of Representatives Standing Committee on Economics
Parliament House
Canberra ACT 2600

Email: economics.reps@aph.gov.au

Dear Ms Owens

Submission - Income Tax (Managed Investment Trust Withholding Tax) Amendment Bill 2012 - Schedule 4 of Tax Laws Amendment (2012 Measures No. 2) Bill 2012

Ernst & Young provides this brief submission to the House Economics Committee on the proposals in the Income Tax (Managed Investment Trust Withholding Tax) Amendment Bill 2012 and schedule 4 of Tax Laws Amendment (2012 Measures No. 2) Bill 2012 to increase the withholding tax rate on fund payments made by Australian managed investment trusts (MITs) to foreign resident investors from 7.5% to 15% from income years commencing on or after 1 July 2012 (the "MITWHT proposals").

We have experienced significant concern from investors and fund managers overseas and in Australia in relation to the MITWHT proposals. This represents the turnaround of a policy which was announced by the Labor government, confirmed in the 2008 Federal Budget and passed in June 2008 in a phased consultative manner. We highlight the need for reconsideration of this proposal and, if the government were to proceed, the need for appropriate transitional measures for investors and project sponsors which have made significant long term financial investments based on this policy.

We have written to urge the government, first, to rethink this measure. This announcement makes foreign investors in Australia nervous and some major investors will rethink their Australian investment plans. Reasons include:

a) The MITWHT will have its greatest impact in relation to attracting foreign investment into Australia's property and infrastructure sectors. The property and infrastructure sectors do not represent "hot money" or speculative capital invested for a short-term; the investments are on a long-term nature, based on long term financial assumptions and of benefit to Australia – in social infrastructure investments, commercial and residential property, roads, ports, electricity and other infrastructure

b) Australia is competing, currently, for global capital investment with other countries. We have seen global asset manager interest in investing into the USA and UK given their lower currency exchange rates and greater turnaround prospects from the global financial crisis and thus potential for higher capital growth. Overseas investors have been prepared to accept slightly lower yields from Australian asset investments given the stability and transparency of our legal, tax and regulatory system. The MITWHT proposals now affect the perception of Australia by global investors

c) The Australian government has a continuing program to position Australia as an Asian regional financial and funds management centre. We support that initiative strongly and the Investment Manager Regime measures being developed. The MITWHT proposals affect perceptions of Australia's tax policy stability and will impact the outcomes of these policies

d) Before the MITWHT, foreign investors were exposed to Australian tax based on their Australian MIT income **net of any investor deductions**. The MIWHT changed this to a final withholding tax on the **gross MIT income of non-residents with no allowance for their outgoings**. The proposals will mean than various investors' Australian tax will be higher than before the MITWHT was introduced

e) Investors' and project sponsors' concerns are exacerbated by the Treasury suggestion to the Business Tax Working Group of potential changes to Australia's thin capitalisation rules.

Some examples of the financial consequences caused by this policy change are:

a) In various Australian MITs, funding existing infrastructure and property projects, foreign investors have had the net yields underwritten for numerous periods including the life of particular projects by the project sponsors, based on the current Australian policy settings. The increase in the Australian MITWHT will be a cost of the project sponsor, will impair the project and in some cases risk causing financial loss to the sponsor

b) There are various prospective projects where the financial structures have been developed and the Australian sponsors have committed substantial funds in establishing the MITs, in legal and financing costs, and which are currently being promoted overseas where the changed MITWHT will have a major impact on the project's economics and viability

We submit that, for Australia to maintain its international reputation as a country with stable tax policy settings which can be relied on when structuring or investing into longer term investments, the government could consider adjustment to the policy: the preferred option would be to reverse the policy. Other options might include the level of the MITWHT or the time when increases are introduced.

If the policy is not reconsidered, there need to be, at minimum, two work streams of action:

1) Consideration of transitional 'grandfathering' measures or potentially phasing in the measures. We recognise that transitional measures would need careful consideration developed in consultation with infrastructure and property sectors. They might include:
   a) Protecting **foreign investors** currently invested in Australian MIT investments (by a grandfathering exclusion and/or phasing in the MITWHT increase)
   b) Protecting (grandfathering) **existing investments** in long term assets namely infrastructure and property investments
2) Review of the significant and onerous integrity measures that limit the application of the MITWHT. When the 7.5% MITWHT was introduced, the Australian government (conscious of revenue risks at that time) restricted the reduced rate only to certain Australian managed funds meeting complex widely held and not closely held conditions to qualify as a MIT. So the low MITWHT was a package - with a changed tax base and new integrity measures: Australia's low MITWHT is not available in numerous situations where, in comparable overseas countries, concessions are available. We submit that any increased MITWHT would require that these restrictions should be reviewed and eased in light of the increase in the rate.

Property Council of Australia submission

We have seen also the public submission of the Property Council of Australia to the Committee. We support that submission.

If you have any queries, please contact Antoinette Elias on 02 8295 6251, Stephen Chubb on 02 8295 6473, Grant Peters on 02 9248 4799 or (for infrastructure issues) Don Green on 02 8295 6473 in the first instance.

Yours faithfully

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