Real Estate Institute of Australia

18 May 2007

Committee Secretary
Senate Economics Committee
Department of the Senate
PO Box 6100
Parliament House
Canberra ACT 2600

Dear Sir/Madam

Please find enclosed the submission by the Real Estate Institute of Australia to the Inquiry into the provisions of tax laws amendment (2007 Measures No.3) Bill 2007.

Yours sincerely

Bryan Stevens
Chief Executive Officer
Real Estate Institute of Australia

Enc:

1. REIA Submission to Inquiry into the Provisions of Tax Laws amendment (2007 Measures No.3) Bill 2007 dated 18 May 2007

PO Box 234, Deakin West ACT 2600
TELEPHONE 02 6282 4277
FACSIMILE 02 6285 2444
EMAIL reia@reiaustralia.com.au
WEB SITE www.reiaustralia.com.au

Real Estate Institute of Australia

REAL ESTATE INSTITUTE OF AUSTRALIA SUBMISSION TO INQUIRY INTO THE PROVISIONS OF TAX LAWS AMENDMENT (2007 MEASURES NO.3) BILL 2007

Proposal

1. The Real Estate Institute of Australia (REIA) proposes that the 30% withholding tax rate on distributions from Australian managed funds to non-resident investors, proposed by the Government in the 2006 Federal Budget, be reduced to a flat and final withholding tax of 12.5%.

Background

2. The REIA is the peak national professional association for the real estate industry in Australia. The REIA has eight members, comprised of the State and Territory Real Estate Institutes, through which about 80% of real estate agencies are collectively represented. The REIA also has key strategic alliances at the national level with the large commercial property companies and major franchisers throughout Australia.

3. Australian Managed Funds manage over $1 billion in total consolidated assets. At both a retail and wholesale level, there is today extensive and growing investment by offshore portfolio investors who may include large institutional investors, pension funds, fund managers and global custodians. Alongside management expertise and innovative products, offshore investors are looking to invest in funds within a tax regime that is competitive and streamlined.

4. Most Australian managed funds are widely-held unit trusts that distribute their income fully, and offer portfolio investments across local and overseas assets (equities, property and bonds). They are taxed on a flow-through basis, providing the ultimate beneficiary with tax treatment comparable to direct investment, but with simpler tax reporting and compliance requirements. These features make them an attractive collective investment vehicle.

5. Regardless of our many advantages, it is also important for Australia to acknowledge the need to be competitive on tax rates in order to attract and maintain offshore clients. Many of our regional competitors recognise the value of the international trade in funds management services, and have introduced more competitive withholding tax rates on distributions to non-resident investors.

6. Currently, foreign investors in Australian property trusts face Australian tax on the trust distributions of 30 percent if the investor is a company, 47 percent if the investor is a super fund and 29 percent to 47 percent if the investor is an individual. These amounts can be reduced if the foreign investor lodges a tax return and claims offsetting deductions. In Budget 2006, the Government announced a general 30 percent withholding tax rate on

Australian source income distributed to non-resident investors, but this change has not yet been enacted.

7. Foreign investors have informed the Australian Funds they strongly favour the international system of a flat and final withholding tax at a competitive rate. They have pointed out the disadvantage of Australia having a headline rate of 30% compared to the rates of Australia's major direct competitors. They consider it more efficient with less compliance costs for the ATO, the Funds and foreign investors.

8. The current tax regime for distributions to non-residents includes a high withholding rate and there is some complexity and regulatory burden in the administrative arrangements for a non-final tax. The effect of the tax rate and the administrative arrangements is that non-residents are deterred form making investments in the Australian market.

9. Some overseas competitors are markedly less with their withholding tax, including Japan has a REIT withholding tax rate of 7% (and nil for super funds), Singapore nil for individuals and 10% for other investors, Hong Kong effective rate of 15% on REIT, as does the US. It is obviously important to promote investment in Australia and we need to promote a competitive tax regime.

10. The 30% rate is non-final and permits the investor to offset it with deductions – which may produce the same net Australian tax costs as a reduced flat rate. But what matters to foreign investors is the headline rate – the compliance costs of lodging Australian tax returns – and the time that it takes to obtain a refund. They consider that the present system, if not changed, will be a major deterrent to foreign investment in Australian Funds.

11. In terms of cost to revenue a new lower tax rate of 12.5 per cent could stimulate further foreign investment in Australian LPTs, increasing the tax base by 7.5 per cent or $23 million. Under certain portfolio adjustment assumptions, this may displace a similar amount from the tax base for dividend income paid to foreign investors, which has a higher estimated average Australian tax rate of 24 per cent. This implies an indirect net loss in revenue from portfolio substitution of $3 million. Combining this with the direct gain to the budget of $2 million under this scenario, gives an overall net loss to the budget of $1 million, as shown in the Econtech Report dated 18 April 2006.

Summary

12. Overall, investment in Australia will be encouraged if there is a competitive withholding tax rate and less administrative inconvenience if that is the final rate. The REIA proposes that the withholding tax rate be set at a flat and final rate of 12.5%.

Prepared by:

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