cutting through complexity

Asia Region Funds Passport

Comparison of withholding taxes

4 February 2016

Contents

Disclaimer

This report has been prepared for the purposes of assisting the Financial Services Council (FSC) with its submissions to Treasury in considering what changes to Australia's withholding tax regime are needed in order to ensure the competitiveness of Australian domiciled funds under the Asia Region Funds Passport regime.

Our comments are made specifically in response to the FSC's request for assistance. Accordingly, neither the firm nor any member or employee of the firm undertakes responsibility in any way whatsoever to any person or company other than the above entity for any errors or omissions in this report, however caused.

The examples provided in the Case Studies and the information provided in the Appendices to this report are for information purposes only and should not be relied upon for the purposes of any advice.

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Executive summary

- Although our asset management industry is the fourth largest in the world, highly skilled, mature and sophisticated, it is not a significant “export industry” for the Australian economy. Disappointingly only 4% of assets are sourced from outside Australia.

- APEC has created a “single market” (ARFP) to enable cross-border fund distribution within the Asian region (APEC members). Australian asset managers will be able to sell their funds directly to retail & institutional investors based in other Asian jurisdictions. Australia now has the *regulatory* framework to internationalise and expand it’s fund industry, establish a regional financial services hub and enjoy an array of economic benefits that will come with fund distribution success.

- However, to achieve this objective Australian managers and their ARFP funds will need to successfully compete with both existing local and other foreign funds, including well regulated, tax neutral (including no WHT on distributions) and simple to understand UCITS funds from Luxembourg and Ireland that have been immensely successful distributing in Asia.

- Taxation has a significant impact on the distribution success of investment funds. We understand that the position of the FSC, as reflected in recent submissions, is that for Australian MIT’s to more effectively compete in Asia, the rate of domestic WHT applicable to distributions made by an Australian ARFP fund to non-resident investors should be limited to a maximum of 5% on all income types (other than franked dividends and non-TAP capital gains). However, even a 5% WHT may, for some Asian distributors and their investor clients, remain a considerable barrier to investment or another hurdle to overcome.

- A more innovative and competitive policy to support this opportunity would be a full WHT exemption on distributions to non-residents. Such a bold tax policy approach, when coupled with a corporate style fund and the greater “speed to market” the ARFP will offer (over a UCITS), could arguably place Australian ARFP funds at a significant competitive advantage over UCITS funds that sometimes suffer greater portfolio WHT than similar Australian funds, due to more advantageous tax treaties.

- Whilst this paper focuses on WHT, other tax issues will need to be addressed in order for Australian success to be achieved (see page 11 below).

Recommendations

Recommendation 1 - A bolder response, placing Australia in the leading position, is an exemption from WHT for Australian ARFP funds

- The FSC believes that to support Australian participating ARFP funds, WHT applied on distributions be limited to 5%. A 5% rate on all income (except franked dividends & non-TAP capital gains) would enhance Australia's competitiveness under the ARFP, beyond what we have seen in recent years (even under the previous MIT WHT regime).

- The ARFP presents significant opportunities for Australian funds to access new capital in an ultra competitive environment, especially from fund structures that apply no WHT on distributions, so we believe a bolder response is necessary.

- Australia must maximize it's advantage of an extensive tax treaty network & information exchange countries. From the perspective of lower rates of WHT imposed on foreign investment income of participating MITs, as compared to UCITS funds sold into Asia. If the rate of WHT on distributions from participating MITs was reduced to nil, this would not only align the taxation of distributions with that of UCITS funds but would result in a **lower overall effective tax rate on distributions**, providing our funds with a **competitive advantage** over UCITS funds and potentially a real "gamechanger for Australia".

Recommendation 2 - Financial modelling be undertaken to compare the projected net overall impact on Government revenue from different WHT rates

- There is a revenue 'trade-off' between a reduced rate of WHT and the increased tax revenue from fund managers, greater industry employment and related service providers from successful ARFP participation. Compare a full WHT exemption, a 5% WHT and retaining the WHT status quo for ARFP MIT's.

Recommendation 3 - Other tax issues should be addressed holistically in order to achieve Australian success under the regime

- Whilst this paper focuses on the current WHT policy settings for MITs participating under the ARFP, these additional tax policy settings form part of an overarching approach and are described below on page 11.

Overview of ARFP regime

Asia Region Funds Passport ("ARFP") – comparative impact of withholding tax

- From 2016, APEC will launch the ARFP, a regulatory framework seeking to enhance the flow of capital, knowledge and consumer choice across the Asian region by creating a "single market" for the distribution of investment funds.
- This paper seeks to examine the comparative impact that withholding taxes (and other taxation), may have on the distribution of investment funds using the "passport" mechanism under the ARFP framework, as well as funds distributed under other regulatory frameworks and bilateral arrangements currently operating in the Asian region.
- Australian ARFP funds will have access to an Asian Host jurisdiction but, will be in direct competition with local funds in the Host jurisdiction (and of course competing with these same local funds if they are "passported" *into* Australia) as well as other foreign ARFP funds, together with funds from other Asian or European jurisdictions by virtue of the other single market initiatives or regulatory agreements that currently operate – see below.
- One could imagine an extremely competitive local market, (which is very good for local investors!) where funds from multiple Asian and European jurisdictions compete with local domestic funds, often using the same bank distribution platforms. In this situation, the impact of withholding tax (or other fund taxation) may have a material impact on the distribution performance of these funds.
- It is true that Australia has a comparatively large asset management industry with approximately $2.6 trillion *(see footnote)* controlled by managed investment schemes. However, and in stark contrast to many other mature capital markets, surprisingly only 3.6% of these assets are sourced from outside Australia *(see footnote).*
- Such a low proportion of foreign sourced assets has long represented a significant weakness of the Australian asset management industry. Australia has not been able to successfully export its sophisticated and mature asset management industry onto the global stage as other jurisdictions have. This is a missed opportunity of significant size. It is hoped the ARFP will provide a mechanism to assist the Australian industry to do so in the future, and part of this will be ensuring the right Regulatory and Revenue settings are in place to support its uptake.

Footnote - 2015 Australian Investment Mangers Cross-Border Flows Report – FSC/Perpetual

Overview of ARFP regime

Asia Region Funds Passport ("ARFP") – comparative impact of withholding taxes

- As mentioned above, in seeking to attract capital from the quickly growing Asian region into Australian funds holding a "passport" under the ARFP, Australian funds will most likely be competing with a range of other foreign funds in the same domestic market due to the:
  - ARFP regime;
  - MRF regime for publicly offered funds between Hong Kong & China;
  - ASEAN passport regime for the recognition of funds between Singapore, Thailand and Malaysia; and
  - UCITS funds currently registered for public distribution in +80 jurisdictions, including all key Asian jurisdictions.
- In order for Australia to export its asset management expertise and develop as a regional finance center, Australian ARFP funds need to be as competitive as possible in each of the Host jurisdictions of the ARFP. Therefore, it is critical that Australia's domestic tax rules do not operate as a material disincentive for local Host market investors to subscribe into Australian funds.
- The current ARFP rules do not address how ARFP funds should be taxed at the fund and investor levels and so existing domestic tax rules will apply, subject to applicable double tax treaties in place between Australia and the target Host jurisdiction.
- The proposed ARFP regime permits Host countries to apply their domestic rules concerning the reporting for tax purposes of members interests (or former members interests) in ARFP funds and each participating country must ensure that the offering of interests in a ARFP fund in a Host country will not create a taxable presence of that fund in the host country.
- This paper therefore compares the withholding and other fund taxes that apply to sample funds domiciled within the ARFP, MRF, ASEAN and UCITS regimes and sold into the ARFP jurisdictions.

Withholding tax policy considerations

Policy considerations

- Many key investment fund jurisdictions impose no tax on income and gains derived by a fund and do not apply WHT on distributions to investors. The Cayman Islands and Bermuda (popular hedge fund domiciles for US fund managers), Guernsey and Jersey (popular fund domiciles for UK fund managers) and Ireland and Luxembourg (the home of cross-border UCITS funds) are the key examples. Some of these jurisdictions also have lighter regulatory regimes.

- Funds domiciled in the above “off-shore” jurisdictions are not part of any regulatory passporting regimes. However, it is worth noting that the European regulatory body (ESMA) has recommended that funds (and their fund managers) located in Jersey and Guernsey be able to join the EU Alternative Investment Fund Managers Directive, the single market regulations for all non-UCITS funds, which includes a passporting regime for alternative funds.

- The “on-shore” fund centres of Luxembourg and Ireland have held a dominant position in the cross-border fund industry for more than 25 years. Whilst numerous factors have contributed to the dominance of Luxembourg, (the largest cross-border fund domicile in the world), and Ireland as the jurisdictions of choice for creating and operating cross-border distributed investment funds, their respective “neutral” tax policies for investment funds have been a key driver of their success.

- The UCITS Directive harmonises product & operator rules on national funds to create a “single market” for creation and distribution of such funds within the EU Member States. However, the Directive does ***not*** attempt to impose harmonised taxation rules on a UCITS fund and the investors in such regulated products.

- Whether or how UCITS funds and their investors are taxed is left totally to the jurisdiction in which the UCITS fund is domiciled, the fund investments held and in which the investors reside. This enables all of the 28 EU Member States to determine and apply their own taxation laws as they pertain to the UCITS funds domiciled in their jurisdiction and together with their local investors. Therefore, there is a wide variation on how UCITS are treated from a tax perspective.

Withholding tax policy considerations

Policy considerations

- Several EU jurisdictions, such as Luxembourg and Ireland, (with small domestic markets), fully exempt investment funds domiciled in their country from tax on income and gains derived from investments held to ensure that the funds are essentially "look through" or tax neutral.

- The most successful of these sold on a cross-border basis is the highly regulated UCITS funds. These funds are sold internationally in more than 80 jurisdictions. The tax treatment of UCITS funds from these two jurisdictions make them significantly more marketable and easier to distribute on a cross-border (although it should be noted that Luxembourg imposes a subscription (or capital) tax of 0.01% to 0.05% on the total net assets of certain UCITS (and other) funds).

- By providing a blanket exemption from tax at the fund and investor level, Luxembourg and Ireland offer distributors and ultimate investors, in whatever jurisdiction, a international fund product, simple to understand, free of any domicile particularities, with a high level of transparency, especially of product taxation, for institutional and retail investors.

- Our experience on the global distribution of cross-border UCITS funds, including into Asia, is that their tax neutrality and simplicity, together with no WHT on distributions, significantly enhances the overall marketability of these funds on a global basis by the many different distribution channels towards both retail and institutional investors wherever they are located. Asian investors are seeking high returning investment funds that do not have complex taxation arrangements, either at the fund level, WHT on distributions or complex arrangements aimed at recovering WHT's suffered.

- By contrast, UK UCITS funds are technically subject to income tax and this arguably gives them better access to tax treaty benefits in respect of withholding taxes suffered in respect of underlying investments, (e.g. US sourced dividend income). However, through a rather complex and cumbersome series of tax calculations UK UCITS funds are also generally free from tax on their income.

- Nevertheless, this specific tax treatment together with the fact that many UK UCITS funds are unit trust structures, makes their distribution process more complex and often more time consuming in many foreign jurisdictions than the processes for Luxembourg and Irish UCITS funds.

Withholding tax policy considerations

Policy considerations (continued)

- Luxembourg and Irish UCITS funds of the corporate form do suffer some tax leakage in respect of specific withholding taxes imposed on their investment portfolios as these funds tend to have access to a fewer number of double tax treaties and thus suffer higher levels of withholding. Alternatively, Luxembourg and Ireland also have fund vehicles that are treated as tax transparent (FCP and CCF respectively) that can enable investors to claim treaty benefits directly.

- Moreover, under the EU Treaty and recent European Court of Justice decisions, many corporate style UCITS funds have been successful at claiming back discriminatory withholding taxes suffered on dividends from investments made cross-border into other EU member states (following the landmark ECJ decision in the 2009 *Aberdeen* case) .

- ARFP funds will be permitted to invest into currency; deposits; depository receipts over gold; transferable securities and money market instruments, and may enter into derivative and securities lending arrangements. ARFP funds are therefore likely to offer equity and debt type products to investors, such as exchange-traded funds, fixed income funds etc, the returns on which will predominantly be dividends, interest and capital gains.

- For non-resident investors, the key tax issues will be:
  - WHT on distributions made from the fund to the investor in respect of Australian sourced income
  - Foreign WHT on dividends and interest derived by the fund; and
  - Capital gains tax on disposal of their interest in the fund.

- Given the range of permitted investments, there is no present need to consider withholding taxes with respect to transactions in real estate or royalties.

- It should be noted that when comparing withholding tax rates between jurisdictions, it is necessary to compare the withholding tax rates that apply to fund vehicles and not general withholding tax rates. For example, Ireland imposes a domestic withholding tax rate of 20% on dividends and interest paid by a resident company (subject to an applicable tax treaty). However, as noted already, no such withholding taxes apply to distributions out of Irish UCITS funds.

Withholding tax policy considerations

Policy considerations (continued)

- The key policy driver for the major European fund centers of Luxembourg, Ireland and the UK to levy nil or nominal taxes on their respective funds was the creation of EU regulations, (a single market) for investment funds in the 1980's.
- Luxembourg had operated an international private banking sector for more than 60 years which evolved into a broader niche financial services industry in the 1970's. In 1982 the European Commission decided to harmonise regulations governing funds aimed at retail investors within the EU. This harmonisation would create a single market for European traditional investment management. The Luxembourg government saw this as an opportunity to further develop their financial services industry and took a number of key policy decisions to position Luxembourg as a future fund domicile hub servicing participants that would utilize the proposed EU Fund Directive.
- With the launch of the 1985 UCITS Directive, Luxembourg was the first country to incorporate the new Directive into their domestic law thus creating an opportunity for fund operators to establish cross-border vehicles. Within the EU framework, Luxembourg also introduced new, innovative, flexible and tax neutral fund structures (that would appeal to investors outside of Luxembourg) to take advantage of the new UCITS Directive, they modernized their domestic regulatory framework and introduced rules and financial assistance to further develop and support local fund servicing entities. Ireland followed and adopted a similar approach to Luxembourg in the early 1990's.
- Importantly, the Governments of both countries have created policies that continue to foster and encourage innovation of fund products that are desirable to the greatest number of investors outside of these countries. These policies also create a tripartite environment whereby, in fulfilling their respective roles, the Government, regulatory authorities and industry participants tend to work towards a common objective of growing their cross-border funds industry by being innovative and agile, seeking to take advantage of market demands and opportunities as they arise. European and international asset managers have rushed to Luxembourg and Ireland to take advantage of this market focused environment.
- The UCITS regulations have been constantly updated (now in its fourth iteration) for new market, governmental and investor requirements, often led by Luxembourg and Ireland. UCITS is today recognised as the global fund brand, the most accepted form of investment fund by regulatory authorities, distributors and investors, (both retail and institutional) in more than 80 jurisdictions.

Other tax policy considerations

Other tax policy considerations

- Both Luxembourg and Ireland now have a +20 year overarching policy objective of making the distribution of their funds as efficient a possible to as many jurisdictions and to the largest number of investor segments as possible on a global basis. In both jurisdictions, the success of UCITS cross-border distribution has driven the constant growth and expansion of their fund servicing industries with a diverse range of international companies with significant employment.
- There have been numerous wider benefits for both local economies of the funds industry growth. The governments have used these industries to showcase their respective jurisdictions, attract multinational companies in other industries and sectors, attract large talented expatriate populations, generate significant government revenue flows from employment, VAT, payroll and associated taxes. In terms of infrastructure, service providers include a plethora of management companies, custodians, fund administrators, accountancy and finance, consulting and law firms and an expanded private banking, family office and wealth management.
- With a deeper and a more diverse range of investment management skills, the UK remained focused on managing the assets gathered by UCITS funds rather than looking to establish a fund or product hub. It has only been recently that the UK, with pressure from the local asset management industry looking at the success of Luxembourg and Ireland, has sought to broaden their asset management industry by seeking to position UK UCITS funds as the preferred cross-border vehicle.
- At the very least, tax policy should be modified to ensure the rate of Australian withholding tax applicable to distributions made by Australian ARFP funds to non-resident investors should be limited to a maximum of 5% on all income types (other than franked dividends and non-TAP capital gains, *see footnote).*
- However, even a 5% WHT may limit Australian ARFP funds from accessing Asian distribution platforms and distribution channels or deter local distributors recommending Australian funds to their investor clients. Many Asian jurisdictions are lower and structurally different tax environments than Australia. As a result many Asian investors may find even a 5% WHT unpalatable, not creditable nor economically recoverable, especially when UCITS fund distributions are free of WHT. With the increasing focus on after tax returns/performance, an Australian ARFP fund fixed income fund may need to outperform a UCITS fund invested in a similar product by a margin that takes account of the 5% withholding tax.

Footnote - FSC letter to Treasury of 10 September 2015

Other tax policy considerations

Other tax policy considerations

- UCITS products have significant brand presence globally and are considered the “gold standard” of international investment funds – regulated under EU law, high levels of investor protection, easy to understand, wide investment choice and tax neutral to fit with local tax rules. UCITS products have a long-term entrenched position of sales success across multiple distribution channels in most of the key capital markets across Asia. We understand that over the past 10 years UCITS funds have attracted more than $US 300 billion from several key Asian jurisdictions. The success of UCITS distribution continues to grow as many UCITS operators open local distribution or sales offices across Asia and local distributors become more familiar with these funds.

- Accessing the ARFP will mean that Australian funds will be competing with UCITS and other Asian region foreign funds. However, what the ARFP offers to Australian asset managers and their passport funds is what UCITS do *not* have in Asia - “speed to market” and this can often be a significant factor in successful distribution, especially where local distributors have clients very eager to invest in a rising market.

- Under the ARFP there will be a 21 day market entry process with precise harmonized requirements. By contrast, the market entry process for UCITS across Asia is un-harmonised and always on a single fund case-by-case ad-hoc basis, often with multiple variables that can slow the registration approval process down. In our experience, in some Asian jurisdictions market entry for UCITS, even from well known asset managers, is restricted and sometimes taking 4-6 months depending on the type of fund, particular characteristics and current administrative practices of the host regulatory authority.

- However, a 5% WHT on distributions when UCITS funds have zero may still place some Australian ARFP funds at a material distribution disadvantage to potential investor segments even taking into account speed to market and before performance is considered. Australia will need to consider fully exempting Australian domiciled ARFP funds from tax on income and gains, and to impose no withholding taxes on the distribution of income and on exit to foreign investors.

- A full exemption from WHT would be the most innovative and boldest policy response to best position Australian ARFP funds at a competitive advantage to local and foreign funds, typically UCITS. A zero WHT on non-resident investor distributions when coupled with the greater “speed-to-market” offered by the ARFP and lower WHT rates on the investment portfolios of some Australian funds as against similar UCITS funds, (due to Australia’s network of double tax treaties), may provide Australian asset managers with a material competitive advantage.

Other tax policy considerations

Other tax policy considerations

- Whilst this paper focuses on withholding tax applicable to non-residents investing in Australian ARFP funds, other tax issues will need to be addressed in order for the ARFP to be successful. These issues include:
  - Providing the same tax treatment of non-resident ARFP funds deriving Australian source income as applies to non-resident investors in Australian ARFP funds, to remove tax discrimination and barriers to investment into Australia;
  - Ensuring that Australian resident investors investing into non-Australian ARFP funds are not subject to tax discrimination;
  - The requirement for Australian ARFP funds under domestic rules to fully distribute income (noting that there is no requirement to do so under the proposed AMIT regime);
  - Developing collective investment vehicles ("CIVs") that are comparable to and more flexible than CIVs used elsewhere and are therefore familiar and potentially attractive to domestic distributors and local investors. This will include considering CIVs structured as corporates (note that more than 80% of Luxembourg UCITS funds are of the corporate style), partnerships and common contractual vehicles, and which should be treated as opaque or flow-through for tax purposes;
  - Considering whether Australian ARFP funds should be exempted from tax on distributions made by investee companies and capital gains realised on the disposal of investee companies; and
  - Whether reporting requirements of investors' interests in ARFP funds should be aligned with the CRS regime.

Case studies - Investor Tax Position (Singapore)

Retail Investor Tax Position

This case study illustrates that a Singaporean retail investor would be subject to greater tax if it invests in Australian bonds via an Australian fund as compared to a local or UCITS fund

Fund domicile

Investment type & location

<u>Case study figures</u>

Bond issue price 100
Coupon (interest) 5%
Acquisition price of investor 95
Gain on redemption 5

Singapore

Bond	Coup.	Red.
Income	5	5
Australian 10% WHT/15% tax (Fund)	(0.5)	(0.75)
Singapore Tax (Investor)	Nil	Nil
Net return	4.5	4.25

Australia

Australian bonds

Assumption that Australian Fund is a Managed Investment Trust (MIT), and redemption gain will be taxable as other income subject to 15% WHT as a fund payment

Singapore

Bond	Coup.	Red.
Income	5	5
Australian 10%WHT/ 15% Tax	(0.5)	Nil
Singapore Tax (Fund)	Nil	Nil
Singapore Tax (Investor)	Nil	Nil
Net return	4.5	5

Singapore

Australian bonds

Redemption (trading) gain will not be subject to Australian tax on basis of tax treaty (no PE) and/or Investment Manager Regime exemption for portfolio gains

Singapore

Bond	Coup.	Red.
Income	5	5
Australian 10% WHT/15% Tax	(0.5)	Nil
Irish Tax (Fund)	Nil	Nil
Singapore Tax (Investor)	Nil	Nil
Net return	4.5	5

Ireland (UCITS)

Australian bonds

Redemption (trading) gain will not be subject to Australian tax on basis of tax treaty (no PE) and/or Investment Manager Regime exemption for portfolio gains

Case studies - Investor Tax Position (Thailand)

Retail Investor Tax Position

This case study illustrates that a Thai investor would be subject to tax if it invests in Australian bonds via an Australian fund as compared to a local or UCITS fund

Thailand

Bond	Coup.	Red.
Income	5	5
Australian 10% WHT/15% tax (Fund)	(0.5)	(0.75)
Thai Tax at 35% with credit for Aust tax (Investor)	(1.25)	(1)
Net return	3.25	3.25

Thailand

Bond	Coup.	Red.
Income	5	5
Australian 10% WHT/15% tax	(0.5)	Nil
Thai WHT at 15%/10% with no credit for Aus tax (Fund)	(0.68)	(0.5)
Thai Tax (Investor)	Nil	Nil
Net return	3.82	4.5

Thailand

Bond	Coup.	Red.
Income	5	5
Australian 10% WHT/15% tax	(0.5)	Nil
Irish Tax (Fund)	Nil	Nil
Thai Tax at (Investor)	Nil	Nil
Net return	4.5	5

Fund domicile

Australia | **Thailand** | **Ireland (UCITS)**

Investment type & location

Case Study figures
Bond issue price 100
Coupon (interest) 5%
Acquisition price of investor 95
Gain on redemption 5

Australian bonds (Australia)

Assumption that Australian Fund is a Managed Investment Trust (MIT), and redemption gain will be taxable as other income subject to 15% WHT as a fund payment.
Foreign source income is only taxable in Thailand if remitted in the year in which the income is derived. If remitted in a later year it is exempt. Assumption remitted/distributed by MIT in income year derived. Potential to remit in later income year if AMIT.

Australian bonds (Thailand)

Redemption (trading) gain will not be subject to Australian tax on basis of tax treaty (no PE) and/or Investment Manager Regime exemption for portfolio gains. Thai funds are not taxable but withhold tax on payments of interest and dividends. Assumption that Thai fund would not receive any tax credit for Aus tax but would need to deduct final withholding tax from payments to Thai resident investors

Australian bonds (Ireland (UCITS))

Redemption (trading) gain will not be subject to Australian tax on basis of tax treaty (no PE) and/or Investment Manager Regime exemption for portfolio gains.
Foreign source income is only taxable in Thailand if remitted in the year in which the income is derived. If remitted in a later year It is exempt. Assumption remitted in later income year by Irish fund as investors can roll up on a gross basis.

Case studies - Investor Tax Position (Korea)

Retail Investor Tax Position

This case study illustrates that a Korean retail investor would be subject to less tax if it invests in Australian bonds via an Australian fund as compared to a local or UCITS fund provided it is entitled to a tax credit in Korea for Australian tax

Korea

Bond	Coup.	Red.
Income	5	5
Australian 10% WHT/15% tax (Fund)	(0.5)	(0.75)
Korean Tax at 15.4% with credit for Aus tax (Investor)	(0.27)	(0.02)
Net return	4.23	4.23

Korea

Bond	Coup.	Red.
Income	5	5
Australian 10% WHT/15% Tax	(0.5)	Nil
Korean WHT at 15.4% with no credit for Aus Tax (Fund)	(0.7)	(0.77)
Korea Tax (Investor)	Nil	Nil
Net return	3.8	4.23

Korea

Bond	Coup.	Red.
Income	5	5
Australian 10% WHT/ 15% Tax	(0.5)	Nil
Irish Tax (Fund)	Nil	Nil
Korean Tax at 15.4% (Investor)	(0.7)	(0.77)
Net return	3.8	4.23

Fund domicile

Australia | **Korea** | **Ireland (UCITS)**

Investment type & location

Australian bonds | **Australian bonds** | **Australian bonds**

Assumption that Australian Fund is a Managed Investment Trust (MIT), and redemption gain will be taxable as other income subject to 15% WHT as a fund payment

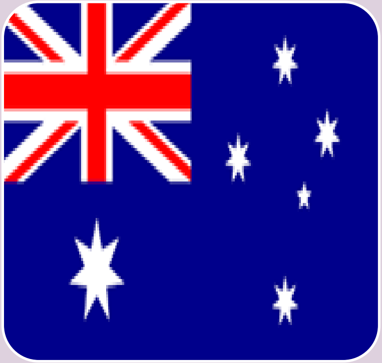
Redemption (trading) gain will not be subject to Australian tax on basis of tax treaty (no PE) and/or Investment Manager Regime exemption for portfolio gains. Assumption that as Korean fund is not taxable, no tax credit for Aus tax can be passed to a Korean investor.

Redemption (trading) gain will not be subject to Australian tax on basis of tax treaty (no PE) and/or Investment Manager Regime exemption for portfolio gains. As Irish fund is not taxable, no tax credit for Aus tax can be passed to Korean investor, on assumption Irish fund is not a flow through vehicle for Korean tax purposes.

<u>Case study figures</u>

Bond issue price 100
Coupon (interest) 5%
Acquisition price of investor 95
Gain on redemption (other income) 5

WHT comparison of Australian funds versus UCITS for non-resident retail investors

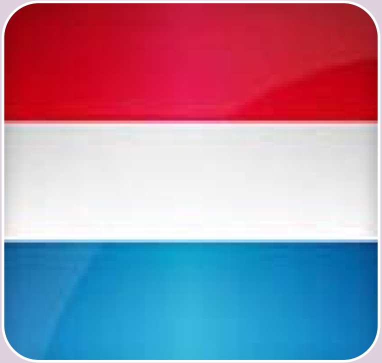


Fund generally non-taxable

WHT on Australian sourced non-franked dividends at 30% (15% if treaty applies) and Interest at 10%.

No WHT on non-Australian source income

No tax on exit if non-TAP gain



UCITS Fund exempt from tax on income and capital gains

No WHT

No tax on exit

UCITS Fund exempt from tax on income and capital gains

No WHT

No tax on exit

Ranking of fund tax regimes for non-resident retail investors

Tax neutral Luxembourg, Ireland, Hong Kong, Singapore	• No tax at fund or investor level • No complex qualifying or calculation rules to achieve tax neutrality • Wide choice of funds
Tax neutral but complex UK, Malaysia	• Complex calculation rules to achieve tax neutrality
Not tax neutral and/or complex/uncertainty China, Australia, Thailand, New Zealand, South Korea, Philippines	• Tax at Fund and/or investor level • Complex qualifying rules (e.g. Australian MIT structures) • Uncertainty in tax treatment (e.g. China)

Appendices

Appendix 1 - WHT comparison of major centres of investment into Australian Managed Investment Trusts

	Japan	NZ	S Korea	China
Australian source Fixed Interest & Cash	**Interest** General - **10%** Financial institution (under tax treaty) - **Nil** **Non-interest income - 15%** (EOI country)	**Interest** General - **10%** Financial institution (under tax treaty) - **Nil** **Non-interest income - 15%** (EOI country)	**Interest** General - **10%** **Non-interest income - 15%** (EOI country)	**Interest** General - **10%** **Non-interest income - 15%** (EOI country)
Australian source Shares (portfolio interest and non-TAP)	**Franked dividends** **Nil** **Unfranked dividends** **10%** (under tax treaty) **Capital Gains - Nil**	**Franked dividends** **Nil** **Unfranked dividends** **15%** (under tax treaty) **Capital Gains - Nil**	**Franked dividends** **Nil** **Unfranked dividends** **15%** (under tax treaty) **Capital Gains - Nil**	**Franked dividends** **Nil** **Unfranked dividends** **15%** (under tax treaty) **Capital Gains - Nil**
Non-Australian source Fixed Interest & Cash	**Interest and non-interest income – Nil**	**Interest and non-interest income – Nil**	**Interest and non-interest income – Nil**	**Interest and non-interest income – Nil**
Non-Australian source Shares (non-TAP)	**Dividends and capital gains – Nil**	**Dividends and capital gains –Nil**	**Dividends and capital gains – Nil**	**Dividends and capital gains – Nil**

Appendix 1 - WHT comparison of major centres of investment into Australian Managed Investment Trusts (cont.)

	USA	Canada	Lux	UK
Australian Fixed Interest & Cash	**Interest** General - **10%** **Non-interest income - 15%** (EOI country)	**Interest** General - **10%** **Non-interest income - 15%** (EOI country)	**Interest** General - **10%** **Non-interest income - 30% /45%** (non-EOI)	**Interest** General - **10%** **Non-interest income - 15%** (EOI country)
Australian Shares (portfolio interest and non-TAP)	**Franked dividends Nil** **Unfranked dividends 15%** (under tax treaty) **Capital Gains - Nil**	**Franked dividends Nil** **Unfranked dividends 15%** (under tax treaty) **Capital Gains - Nil**	**Franked dividends Nil** **Unfranked dividends 30%/45%** (no tax treaty) **Capital Gains - Nil**	**Franked dividends Nil** **Unfranked dividends 15%** (under tax treaty) **Capital Gains - Nil**
Non-Australian Fixed Interest & Cash	**Interest and non-interest income – Nil**	**Interest and non-interest income – Nil**	**Interest and non-interest income – Nil**	**Interest and non-interest income – Nil**
Non-Australian Shares (non-TAP)	**Dividends and capital gains – Nil**	**Dividends and capital gains –Nil**	**Dividends and capital gains – Nil**	**Dividends and capital gains – Nil**

Appendix 2 - WHT comparison of UCITS domiciled funds in Europe

	UK	Ireland	Luxembourg
Structure of domestic funds	▪ Authorised Investment Fund (Open ended investment company or authorised investment trust) ▪ Authorised contractual scheme (co-ownership or partnership)	▪ Variable capital investment company ▪ Unit trust ▪ Common contractual fund ▪ Investment Limited partnership	▪ SICAV ▪ FCP ▪ Limited partnership
Fund level tax on profits and gains	**OEICs/AUTs** ▪ Subject to tax at 20% on taxable income but dividend income received by **equity funds** (domestic and overseas) is exempt and interest distributions made by **bond funds** are deductible, so in practice should generally not have any net taxable income ▪ Funds with mixture of dividend and interest income (but which do not qualify as bond funds) can elect to be treated as a **tax elected fund**, such that the point of taxation is moved to the investor. ▪ These funds are not taxed on capital gains **Co-ownership and partnership contractual schemes** are tax transparent	None	None
WHT on Fund distributions to non-resident retail investors	**OEICs/AUTs** ▪ No WHT on dividends paid by equity and tax elected funds ▪ No WHT on interest distributions by bond fund and non-dividend (interest) distributions by tax elected fund provided declaration of non-residence provided. If invest via reputable intermediary, no WHT if manager has reason to believe investor is non-resident. If WHT (at 20%) deducted, may be able to be reclaimed under relevant tax treaty.	No WHT	No WHT
Capital gains tax on exit by non-resident retail investors	None	None	None

Appendix 3 - WHT comparison of ASEAN domiciled funds

	Singapore	Thailand	Malaysia
Structure of domestic funds	▪ Company, unit trust or limited partnership	▪ Unit trusts	▪ Unit trusts
Fund level tax on profits and gains	▪ Exempt from tax on qualifying income and gains – covers most types of marketable securities and alternative asset classes (except Singapore real estate)	▪ Not subject to corporate income tax	▪ Subject to income tax rate of 25% but in practice not taxable as most of the income received by unit trusts is not taxed.
WHT on Fund income distributions to non-resident retail investors	▪ None	▪ Non-resident corporates are not subject to tax on 'profit sharing' ▪ Non-resident individuals are assessable and subject to tax at progressive rates of 0% to 35%.	▪ As unit trusts are generally not taxable, distributions to non-residents are also non-taxable
Capital gains tax on exit by non-resident retail investors	▪ None	▪ None	▪ None

Appendix 4 - WHT comparison of ARFP domiciled funds not in ASEAN

	Australia	New Zealand	South Korea	Philippines
Structure of domestic funds	▪ Unit Trusts	▪ Unit Trusts	▪ Trust or entity type	▪ Revocable trust fund
Fund level tax on profits and gains	▪ Non-taxable	▪ Non taxable if elect into Portfolio Investment Regime (“PIE”)	▪ Trust is not taxable ▪ Entity type is assessable but can deduct dividends where dividend exceeds 90% of distributable income	▪ Considered to be a flow through entity
WHT on Fund distributions to non-resident retail investors	▪ Franked dividends nil ▪ Unfranked dividends 30% but generally reduced to 15% if a tax treaty applies ▪ Interest 10%	▪ In principle, taxed at 28% on taxable income of the fund allocated to the investor, but in practice the allocated income will be deemed 5% income on Foreign Investment Fund interests and Australian listed shares. There is no WHT on fully imputed NZ source dividends ▪ Funds targeted at foreign investors can elect to be Foreign Investment PIEs, in which case no WHT provided fund does not hold New Zealand assets	▪ Korean source dividends and interest – generally 22%, subject to an applicable tax treaty	▪ Dividends – 20% ▪ Interest on bonds, deposits – 20%
Capital gains tax on exit by non-resident retail investors	▪ Exempt provided non-TAP gain	▪ None	▪ None	▪ Gain on sale of unlisted domestic shares – 10%

Appendix 5 - WHT comparison of MRF domiciled funds

	Mainland China	Hong Kong
Structure of domestic funds	▪ Securities Investment Fund ▪ **Neither the Ministry of Finance nor the State Administration of Taxation has released tax circulars regarding tax issues relating to MRFs. The information in this table is therefore based on existing tax regulations that apply to SIFs established in mainland China that invest in mainland China securities**	▪ SFC authorised funds
Fund level tax on profits and gains	▪ SIFs are temporarily exempt from corporate income tax in respect of gains realised from trading of shares and bonds, dividends and distributions from shares, interest from bonds and other income ▪ SIFs are temporarily exempt from business tax in respect of gains realised from the trading of shares and bonds.	▪ SFC authorised funds are exempt from HK profits tax
WHT on distributions to retail investors	▪ Corporate investors in SIFs are temporarily exempt from corporate income tax ▪ Individual investors are temporarily exempt from individual income tax and business tax in respect of distributions	▪ There are no withholding taxes in Hong Kong
Capital gains tax on exit by non-resident retail investors	▪ Individual investors are temporarily exempt from individual income tax and business tax	▪ None

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