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Regulatory Powers and Accountability Unit
Financial System Division
The Treasury
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AIMA AUSTRALIA SUBMISSION to the Australian Treasury's Consultation on the Corporate Collective Investment Vehicles - Regulatory and Tax Frameworks

About AIMA

AIMA, the Alternative Investment Management Association, is the global representative of the alternative investment industry, with more than 2,000 corporate members in over 60 countries. AIMA's fund manager members collectively manage more than $2 trillion in assets. AIMA draws upon the expertise and diversity of its membership to provide leadership in industry initiatives such as advocacy, policy and regulatory engagement, educational programmes and sound practice guides. Many of AIMA's offshore members currently operate under the sufficient equivalence relief. In addition AIMA has over 150 local based corporate members including managers and key service providers. For further information, please visit AIMA's website, www.aima.org.

As an industry body whose membership is predominantly that of private fund managers, we take a keen interest in the development and enhancement of this part of the industry as well as the asset management industry more broadly. It is with this perspective that we make some additional recommendations for Treasury's consideration.

Executive summary

AIMA strongly supports the Government's proposal to introduce a broader range of tax flow-through vehicles to compete more effectively with similar vehicles successfully used throughout Europe and North America, and more recently, the Singapore Variable Capital Company (**VCC**) and the Hong Kong Open-ended Fund Company (**OFC**) vehicles introduced by Singapore and Hong Kong respectively. The unique structural requirements of Australia's managed funds, which are not commonly used or understood by foreign investors, put Australian fund managers at a commercial disadvantage. Many Australian hedge fund managers establish offshore funds to attract offshore investors because the current unit trust structure is not well understood by offshore investors. Having a fund structure that could be used for both domestic investors and offshore investors would be welcomed by AIMA members and stimulate growth in the volume of foreign assets managed by Australian managers.

The revised exposure draft legislation for the CCIV, released by Treasury for comment on 27 August 2021, has dealt with some issues raised by industry in the 2017 and 2019 consultations. We particularly welcome the changes to:

(a) remove the requirements for retail CCIVs to have an independent depository;

(b) allowing cross-investing between sub-funds;

(c) Elimination of non-creditable penalty tax payable of failure of the widely held test;
;

(d) Removal of proposals to remove CGT discount at the CCIV level, although we note this may still be introduced in proposed but still unlegislated AMIT changes

(e) Removal of new penalty for attribution ‘unders and overs’ that result from a lack of reasonable care.

However, there remain some issues which may impede the success of CCIVs and their ability to truly compete on a global scale. We believe it is critical that these concepts are considered and further refined in order to enable the success of the CCIV regime. Treasury should recognise the reality that where fund managers and promoters are deciding where a fund is to be established, they are likely to choose the most flexible, efficient, cost effective and tax neutral vehicle which meets their investors’ needs. If Australia wishes to gain traction for its CCIV regime, Australia should allow for a time and cost efficient set up and maintenance of structures, particularly in relation to wholesale funds.

As a general comment, we also note the draft legislation is more extensive and more prescriptive than certain other jurisdictions, for example Singapore where their adoption of the VCC regime appears to have been successful with 370 VCCs launched since 2020, and is also more extensive than the current Australian registered MIS regime.

It is important to note other jurisdictions are taking active steps to ensure that their regime for variable capital companies meet the needs of managers and investors in their attempt to set their jurisdiction apart as a preferred jurisdiction for the domicile of private funds. For example, to encourage fund managers to adopt the VCC, the Monetary Authority of Singapore (**MAS**) has introduced a VCC Grant Scheme to help to meet the incorporation and registration costs involved with a VCC where the MAS will co-fund up to 70% of eligible expenses that are paid to Singapore-based service providers up to a maximum of SGD150,000 for each application, with a maximum of three VCC per fund manager. Hong Kong also offers similar grants with respect to their promotion of the OFC regime.

CCIV – treatment of wholesale funds

To bolster the ability of the CCIV to be able to truly compete on a global scale, AIMA considers it is critical that certain requirements applicable to registered schemes but not unregistered wholesale schemes are not replicated to apply to wholesale CCIVs. Unless there is a policy reason for imposing additional regulatory requirements on wholesale vehicles, AIMA views these as unnecessarily burdensome on wholesale CCIVs, particularly in comparison to the existing wholesale managed investment scheme in Australia. These include the following requirements:

(a) duties of the director to act in the best interests of members and treat members equally (section 1224D). These are appropriate duties for retail schemes however go beyond general trust law requirements and may restrict the flexibility typically afforded to wholesale investors by the ability to contract for wholesale schemes;

(b) corporate director to be a public company (section 1224F);

(c) requirement for a members’ meeting and special resolution for the retirement or replacement of the corporate director (section 1224T and 1224U). Currently, the constitutions of wholesale managed investment schemes usually set out the process for retirement and replacement of a trustee. A similar approach could be taken for wholesale CCIVs;

(d) application of provisions prescribing the process and requirements of meetings of a CCIV including the ability for members to request a meeting in Part 2G.4 (section 1229A – 1229G). AIMA queries the rationale for requiring such prescribed processes usually applicable only to registered schemes. Particularly problematic is:

(i) the obligation for corporate directors to hold meetings on request of members with 5% of votes would be unattractive for wholesale fund managers; and

(ii) prohibiting corporate directors and their associates from voting with respect to a wholesale CCIV does not work especially where fund managers are invested (this is common for co-investment situations).

Amending the constitution

The constitution of a retail CCIV may be modified only by special resolution of members, or by the corporate director if the corporate director reasonably considers the change will not adversely affect members' rights (section 1223D). This reflects the current standard for registered schemes which has proven to be problematic where technical adherence to this standard leads to an outcome which is not in members' best interests. AIMA suggests the more appropriate standard could be to allow the corporate director to make changes that will not ***materially adversely*** affect members' rights, and where members are given 30 days' notice of the proposed change to enable voluntary redemptions.

Under the proposed section 1223C, ASIC has the power to direct a retail CCIV to modify its constitution to ensure that the CCIV's constitution complies with the content requirements. This may be problematic where investors have already invested into the CCIV on the basis of the terms in the original constitution.

PDS exemptions not sufficiently applied

AIMA notes certain exemptions from the requirement to provide a PDS normally applicable to managed investment schemes (as set out in sections 1012D – 1012E of the Corporations Act) have not been applied to CCIVs. This includes:

(a) where the investor has already received a PDS containing all the information the PDS would be required to contain (section 1012D(1));

(b) where the investor is an existing investor and already has all the required information (section 1012D(2));

(c) in respect of an offer made under a takeover bid (section 1012D(7));

(d) in respect of a rights issue (section 1012DAA(2)); and

(e) in respect of indirect issues (section 1012DA).

AIMA considers these situations may equally apply to CCIVs. Unless there is a reason for disapplying these exemptions (and therefore resulting in different requirements as applicable to provision of PDS for managed investment schemes), AIMA suggest a consistent approach should be adopted for the requirements to provide a PDS.

Listing of CCIVs

Given that retail CCIVs (with only one sub-fund) will be able to be listed on prescribed financial markets, we query how the buy back prohibition would work (section 1231T and 1231Z). AIMA suggests that Treasury reconsider the buy back prohibition, with reference made to the concepts of on-market buy backs by listed trusts and the internal market-making of exchange traded managed funds. AIMA considers it is important to allow for CCIVs to provide sufficient liquidity for investors.

The insider trading exception (section 1244ZA) with respect to member's withdrawal for buy backs calculated by reference to the underlying value of assets does not contemplate redemptions from listed CCIVs. AIMA suggests reference needs to be made also to the market price of shares on redemption to facilitate on market buy backs/internal market making.

Sub-fund design

AIMA supports the clarification made to refer only to Australian courts in relation to the Court's power to determine the assets and liabilities of the sub-fund (section 1233H). However, AIMA is still concerned that the Court's power to "make any order it considers appropriate" in relation to assets and liabilities of the sub-fund does not provide sufficient certainty for investors and counterparties (section 1236E).

Maintenance of capital rules

Given that sub-funds are intended to be able to act as open-ended investment funds with variable capital and will allow redemptions and have capital that varies from time to time, AIMA queries the need for extensive provisions regarding capital reductions, buy-backs and self-acquisition in addition to the provisions relating to the redemption of shares. We note that this compares unfavourably with both the existing framework for registered managed investment schemes and other jurisdictions like Singapore. This is an example of where the magnitude and complexity of the proposed rules jeopardise the potential of the CCIV as managers will not be inclined to adopt a fund vehicle where, all other things being equal, there will be additional time and costs incurred in establishing and operating the vehicle compared to alternatives.

AIMA submits that the capital reduction and self-acquisition rules should not apply generally to CCIVs, as they are not appropriate for open-ended investment funds.

CCIV – Tax Treatment

The comments below focus on the more significant tax issues with the current draft CCIV tax proposals.

The key aim of the CCIV proposal was to help Australia develop as a regional financial services hub with internationally competitive tax laws, in order to drive further opportunities and growth from foreign investment using the services of Australian managers.

An underlying focus of the current draft of the proposed CCIV tax law appears to be to protect the Australian tax base by applying the same restrictive qualification rules as for AMITs and to impose the same complex withholding tax rules and high rates of non-resident withholding tax on investors in CCIVs as are imposed on investors in AMITs.

During consultations it has been articulated that the aim of the current CCIV tax rules is to achieve an equivalent tax result for investors in CCIVs as compared to AMITs. Unfortunately this approach is not helpful for the following reasons:

- the unfamiliarity of trusts to global investors who typically seek to make investments via more familiar corporate vehicles;
- the application of complex, restrictive and uncertain widely held tests for funds to qualify as CCIVs;
- the potential for CCIVs to default to Division 6 trust taxation, which is a flawed model for the taxation of modern day collective investment vehicles which the Government acknowledged in 2016 when it encouraged the industry to move away from Division 6 trusts to the AMIT regime; and

- the very unattractive non-resident withholding tax rates applicable to AMITs and to Divisions 6 trusts and therefore to CCIVs of up to 45% compared to zero withholding applicable to competing vehicles.

Furthermore, the current lack of income tax, CGT and stamp duty rollover relief for existing funds seeking to transition to CCIVs will likely result in no existing funds being transitioned to the CCIV regime.

The proposed CCIV tax rules as drafted continue to compare unfavourably against the tax arrangements for competing foreign collective investment vehicle regimes such as UK OEICs, Luxembourg SICAVs, Singapore Variable Capital Companies (VCC), Hong Kong open-ended fund company (OFC) and ASEAN Collective Investment Schemes. This unfavourable comparison specifically relates to:

(i) the Australian CCIV regime is the only regime which requires the satisfaction of complex widely held tests;
(ii) the withholding tax exemptions afforded for all income for most of the competing vehicles;
(iii) the corporate nature for international tax purposes of all of these vehicles except CCIVs.

The successful expansion of Australia's fund management industry to service CCIV funds would increase Australia's tax revenue from taxing the profits of the expanded Australian businesses and from taxation of additional Australian employees.

To the extent that the above factors dampen or fail to produce new foreign investment then little to no increased revenue will be generated from the proposed CCIV regime.

Given the increasing familiarity of at least wholesale foreign investors with investing into AMITs, the current approach will likely see little take up by Australian fund managers. This is because there will be no appreciable tax rationale for foreign investors to choose a CCIV over an AMIT given both vehicles are intended to have exactly the same tax features.

Contact points

We would be happy to discuss any aspect of our submission or provide further information to Treasury.

The AIMA contacts in respect of this Submission are:

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Yours faithfully

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