KPMG Australia submission

Treasury Laws Amendment (Corporate Collective Investment Vehicle) Bill 2021

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24 September 2021
This report contains 18 pages
KPMG Submission - Treasury Laws Amendment (Corporate Collective Investment Vehicle) Bill 2021(66362033.2)

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Executive Summary

KPMG Australia ("KPMG") appreciates the opportunity to comment in relation to the Regulatory Framework and Tax Framework components of the *Treasury Laws Amendment (Corporate Collective Investment Vehicle) Bill 2021* ("the Bill").

We support the Bill's objective of introducing an investment vehicle with a legal structure that foreign investors are likely to better understand when compared to a unit trust, but which retains the flow-through taxation attribute of a unit trust. We welcome the simplified frameworks that the Bill proposes.

Our recommendations are targeted at areas where greater certainty could be provided to fund managers and potential investors. If fund managers are to establish and promote a corporate collective investment vehicle ("CCIV"), it would be important that they can convey with reasonable certainty the legal and taxation features of the CCIV to potential investors. We would welcome a swift resolution of these matters in order that managers and service providers can have as much lead-time as possible to develop their offerings prior to the framework's commencement on 1 July 2022.

Regulatory Framework:

- The CCIV is intended to be a variable capital investment vehicle. It is therefore vital that the Bill aligns the CCIV to work the same way as a managed investment scheme, without any capital reduction or maintenance rules applying.
- The Bill should remove unnecessary additional requirements on wholesale CCIVs and enable more flexibility for wholesale CCIVs in line with the existing requirements and flexibilities available for a wholesale unit trust.
- It is highly desirable for the Government to announce that it is committed to facilitating the transition of existing managed funds into the CCIV regime and

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to consequently either include the necessary provisions in the Bill or provide a strong message that will facilitate a funds industry wide consideration of the use of the CCIV regime for existing product ranges by way of conversion.

Tax Framework

- As a priority, the Bill should address the tax consequences of a managed investment trust (“MIT”) transitioning to CCIV status. This should include the rollover of membership interests, CGT and revenue assets of the MIT. It should include the MIT’s inherited history of losses, tax elections and choices, the 45-day rule and controlled foreign company (“CFC”) attribution accounts.
- The Explanatory Memorandum (“EM”) to the Bill should state the government’s expectation of the consequences where the aggregate Australian withholding tax on a CCIV distribution exceeds the amount that a treaty partner jurisdiction would expect to be due on a legal form dividend.
- Treasury should consider whether there may be any unintended outcomes of the “deemed trust” treatment of a CCIV sub-fund as a result of the permanent establishment that may arise for an investor that is a deemed beneficiary.
- The Bill provides that an investor in a CCIV sub-fund which does not qualify for AMIT treatment can be in a worse position than an investor in a Division 6 trust with similar beneficiary entitlements. This would occur in the case of income that the CCIV had not distributed by the end of the income year, and which would then be taxed on the deemed trustee at the highest marginal rate. This can be addressed by allowing the CCIV an adequate period of time following year-end to make a catch-up distribution, or by applying Division 6 rules on present entitlement.
- We urge the government to progress the legislative framework for a flow-through limited partnership CIV, which it had first proposed around the same time as initiating the design of the CCIV framework.

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KPMG comments

1 General

KPMG welcomes the opportunity to comment on Regulatory Framework and Tax Framework components of the *Treasury Laws Amendment (Corporate Collective Investment Vehicle) Bill 2021* (“the Bill”).

- The measures included in the Bill are welcome in that the CCIV provides an additional option for Australian fund managers that may assist them in attracting foreign and domestic investors. The changes that the government has made to the proposed frameworks since the initial consultations in 2017 are positive and should provide greater simplicity for market participants and their advisers.

- For investors to have confidence in investing in a CCIV, it is important that they have a reasonable level of certainty as to the legal and taxation outcomes. In particular, the interaction of the Australian tax system with the tax system in the investor’s country of residence will need to be able to be clearly understood.

- It is also important for the success of the CCIV policy that investors in a CCIV should have tax and regulatory outcomes that are not inferior to those obtained by investors in an AMIT. The ease with which a current AMIT can transition to a CCIV structure will also be fundamental to the extent of usage of the CCIV.

- Our comments on the Bill focus on areas where the government should consider modifications to the Bill in order to achieve the objectives which we have set out in 1.2 and 1.3.

- Section 2 includes our comments on the regulatory framework. Section 3 includes our comments on the tax framework. Appendix A includes our responses to the specific consultation questions included in the explanatory materials to the regulatory framework.

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2 Regulatory Framework

2.1. *Depositaries*

- We welcome the decision not to require the CCIV to have a depository.

2.2. *Cross-investing*

- Our responses to the specific questions regarding cross-investment appear elsewhere in the submission. Cross-investment is a welcome flexibility under the Bill.

- The common law two-party rule does present practical issues for a responsible entity ("**RE**") of two schemes that wishes to contract with itself in its separate RE capacities. This common rule is managed in a managed investment scheme, and it would be desirable if the Bill could include a specific provision that enabled a CCIV to contract with itself where the contract is referrable to two different sub-funds of the CCIV.

2.3. *Variable capital company*

- The CCIV is effectively intended to be a variable capital investment vehicle. In order to align the CCIV and a sub-fund to work the same way as a managed investment scheme without any capital reduction/ maintenance rules applying, we recommend the following changes:

  - Capital distributions should be able to be made at any time at the discretion of the corporate director for a sub-fund, so that the sub-fund operates in a comparable way to a managed investment scheme. This includes allowing withdrawals pursuant to liquidity events and compulsory withdrawal mechanisms (e.g. because of investor default).

  - A buy-back of shares on-market should be facilitated to align with how an ASX-listed managed investment scheme operates. The same approach should apply to an unlisted CCIV who may choose to buy-back and cancel shares rather than implement a redemption.

2.4. *Redemption pricing*

- We recommend that the Bill should provide that the formula for redemption price of a share referrable to a sub-fund is to be set out in the constitution of the CCIV, along with the redemption price valuation timing. This then aligns with the existing managed investment scheme regime and allows the market to price the units in a way that is appropriate for the product. This includes in most cases, adjusting the price by a transaction cost factor.

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- In addition, the Bill should contemplate redemption mechanics in terms of the time frame for satisfying a redemption and the ability to introduce into the constitution qualifications on the redemption period to enable a free redemption period or an extension due to a market dislocation event etc. This includes aligning the Bill's requirements for redemptions in retail CCIVs in section 601KA and section 601GA (4) of the *Corporations Act* for registered managed investment schemes.

2.5. *Amending the constitution of a CCIV and ASIC powers*

- We recommend that if a proposed change to a retail CCIV constitution would only affect the shareholders who hold shares referrable to one sub-fund, then only those members should be required to pass a special resolution to make the change.

- We recommend that the proposed ASIC power to direct changes to retail CCIV constitutions should be removed. This power does not currently exist in relation to registered schemes. It is a power which could be used to re-write the bargain that the investors and the CCIV have concluded. ASIC already has adequate powers to exercise if it was concerned about the contents of a CCIV's constitution.

2.6. *Corporate director should be a "wholesale client"*

- We recommend that the Bill should clearly state that a CCIV is to be treated as a "wholesale client" for purposes of Chapter 7. This would align the treatment of the licensed corporate director with the treatment of a licensed RE of a registered scheme.

2.7. *Duty to act in the best interests of the CCIV*

- We recommend that the duty to act in the best interests of the CCIV should be to act in the best interests of the shareholders who hold shares referrable to a sub-fund.

2.8. *Wholesale CCIVs*

- We recommend certain changes which are all designed to remove unnecessary additional requirements on wholesale CCIVs and enable more flexibility for wholesale CCIVs in line with the existing requirements and flexibilities available for a wholesale unit trust. These include:
    - The duties of the directors of a corporate director of a wholesale CCIV should be no more onerous than for a wholesale trust. The

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Bill proposes an extension of the statutory duties to wholesale CCIVs, which is the imposition of retail standard duties on a wholesale vehicle. As an alternative, if a corporate director of a wholesale CCIV is to be subject to statutory duties, then those duties should be capable of being contracted out of.

- The corporate director of a wholesale CCIV should be able to retire or be removed in accordance with the CCIV's constitution. This could be with or without a meeting of investors, where all investors are wholesale.
- Wholesale CCIVs should be free to provide in their constitution for their own arrangements and processes for shareholder meetings.
- Wholesale CCIVs should not be subject to the voting prohibitions in section 253E of the *Corporations Act*.
- A corporate director of a wholesale CCIV may be a private company or a public company.

2.9 *Transition*

- The Bill does not yet include any reference to the Government's position on transition of existing managed funds into the CCIV regime. It would be highly desirable if the Government announced its commitment to allowing for this transition. This strong message would help facilitate a funds industry-wide consideration of the use of the CCIV regime for existing product ranges by way of conversion.
- A corporate director of a CCIV will require an AFS licence to operate the CCIV. We understand that ASIC is cooperating with the Treasury regarding the development of the CCIV regime. We also understand that ASIC has previously indicated that it intends to facilitate an existing licensed RE being able to vary its AFS licence to become a corporate director on a "fast-tracked" basis. This ASIC support will also be an important part of a transition regime for the existing funds industry.

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3 Tax Framework

3.1. *Transition from an attribution managed investment trust ("AMIT") to a CCIV*

- We recommend that there be rollover provisions covering the transition of an AMIT by way of transferring its CGT and revenue assets to a sub-fund of a CCIV.

- It would be helpful for taxpayers if the Explanatory Memorandum to the Bill could confirm that Subdivision 126-G and section 115-30 *Income Tax Assessment Act 1997* ("ITAA 97") are intended to apply such that the CCIV sub-fund would take on the AMIT's cost base and original acquisition date for capital gains purposes in respect of the AMIT's CGT assets which are transferred to the sub-fund.

- In order to reduce barriers to transition, the CCIV sub-fund should also be able to inherit the transferring AMIT's brought forward capital losses and revenue losses. Treasury should consider including relevant provisions in the Bill.

- Further, there should be provisions allowing the CCIV sub-fund to inherit the AMIT's various tax elections and choices, as well as ensuring continuity of tax attributes such as the 45-day rule and attribution account credit balance in respect of attributed income under the controlled foreign company ("CFC") provisions. Treasury will need to balance the benefit of ensuring continuity in tax attributes with the maintenance of integrity in the tax system.

3.2. *Interaction with Australia's double taxation agreements*

- The treatment of each sub-fund of a CCIV as a deemed trust for Australian income tax purposes will result in certain withholding tax ("WHT") outcomes. It is possible that the WHT applying to a CCIV distribution may exceed the rate of tax that a foreign tax authority may consider should apply under one of Australia's bilateral tax agreements to what is a legal form dividend.

- Treasury should provide commentary on what outcomes it would expect in this situation. If it is the case that Treasury would not expect to refund the foreign resident taxpayer the difference between the WHT amount and the Australian tax rate applicable to a dividend under the treaty, then it should clearly state this in the explanatory material.

- For example, while it may be rare for one foreign resident taxpayer to have an interest of more than 10 percent in a CCIV, the AMIT rate of WHT may

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exceed the rate specified for a non-portfolio dividend in one of Australia's bilateral tax agreements (which could be as low as 5 percent).

3.3. *Treatment of CCIV sub-funds that do not qualify as an AMIT*

- It is possible that a CCIV sub-fund may not qualify as an AMIT for reasons unrelated to the actions or decisions of the CCIV itself, and that the CCIV would not be able to take advantage of the temporary non-qualification concessions in the legislation.

- Proposed section 195-125 deems an investor in a CCIV sub-fund to be presently entitled to so much of the net income of the deemed trust as is represented by the distributions that the investor receives during a year of income.

- It may not be practically possible for a sub-fund to distribute all of its net income before the end of the income year, even though it may have attributed all such income to unitholders in its records and created what would typically have been a present entitlement for the purposes of Division 6 ITAA 36.

- Therefore, an investor in a CCIV sub-fund assessable under Division 6 may be at a disadvantage to a unitholder in a standard Division 6 trust, in that income to which the investor is presently entitled but which is not distributed by year-end could be taxed on the CCIV at the top marginal rate.

- One alternative would be to expand the scope of proposed section 195-125 to have present entitlement include income attributed to the investor by year-end and distributed within a reasonable timeframe thereafter (say, three months, which aligns with the current AMMA statement timeframe). Another alternative would be to allow the deemed present entitlement rule in section 95A ITAA 36 to apply to the sub-fund.

3.4. *Deemed permanent establishment created through CCIV investment*

- Subsection 3(11) *International Tax Agreements Act 1953*, or alternately the business profits article of one of Australia's bilateral tax agreements, may deem a permanent establishment in Australia to arise for an investor who has an interest in a deemed trust which is carrying on a business in Australia.

- Treasury should consider whether there may be any unintended consequences from the interaction of the deemed trust status of the CCIV with these other provisions.

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3.5. *Proposed introduction of tax framework for a flow-through limited partnership vehicle*

- A limited partnership investment vehicle with flow-through taxation treatment was also on Treasury’s agenda when the CCIV consultation process commenced in 2017.
- Limited partnership vehicles are also well understood by foreign investors and may be more attractive than a CCIV for investors in infrastructure or real estate.
- Therefore, it would complement the CCIV very well if the limited partnership vehicle could be prioritized over the coming months so that foreign investors and Australian fund managers have a comprehensive suite of investment vehicles from which to select.

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A Appendix A: Responses to consultation questions on the regulatory framework

KPMG Law Submissions on Exposure Draft legislation on Corporate collective investment vehicle

24 September 2021

Consultation Questions	KPMG Law Comment
Requirements or restrictions on cross-investment within a CCIV	
1. How should circular investment be prevented in Regulations? a. Some jurisdictions include requirements to prevent a sub-fund that has been cross-invested into by a sub-fund in the CCIV from cross-investing in another sub-fund of the CCIV. This effectively ensures there is only 'one layer' of cross-investment with the CCIV. b. Would similar restrictions be appropriate in the Australian context?	Some jurisdictions do include restrictions on more than 'one layer' of cross-investment with the CCIV, e.g. UK OEIC, but some jurisdictions do not, e.g. Singapore VCC. We recommend that there should be no restrictions on circular investments since managed investment schemes are not subject to such restriction. We submit that having the power to impose the restriction in the regulations would be a satisfactory compromise.
2. Should cross-investment be facilitated up to a certain level or limit? a. Some jurisdictions restrict cross-investment over certain levels or thresholds within the vehicle or	The cross-investment should not only be facilitated up to a certain level or limit. We are aware that in some jurisdictions such as Malta, the cross sub-fund investment is permitted subject to a cap across all sub-funds of the same umbrella fund. In other jurisdictions, there is no such limit.

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Consultation Questions	KPMG Law Comment
within a protected cell. Should similar limits be included in the Australian context? b. Should different limits apply depending on whether a CCIV is a retail or wholesale CCIV?	We submit that if the Government considers that there should be a level or limit imposed on cross-investment of a retail CCIV, there should be no such limit on the wholesale CCIV, given the wholesale CCIV is a lightly regulated investment vehicle.
3. How will the associated transactions relating to cross-investment be reflected in financial records and reports prepared for the CCIV? a. How will these records and reports be audited and checked to ensure these transactions are appropriately reconciled? b. How will these records and reports be made available to investors?	We see no reason why cross-investments should not be reflected in financial records and reports in the same way that cross-investment is so reflected in a MIS cross-investment model.
Material covered in Product Disclosure Statements and constitutions	
4. Are the requirements to ensure the constitution of a retail CCIV and relevant Product Disclosure Statements contain material in relation to cross-investment appropriate and sufficient?	It should be clarified that a PDS can be prepared for an offer of shares referable to a particular sub-fund, not necessarily a PDS for the whole CCIV. Otherwise, we believe the requirements are adequate.
Membership rights By acquiring shares that relate to a sub-fund of the CCIV, the CCIV obtains rights as a member of that sub-fund and the CCIV. Treasury is seeking feedback on the appropriate adjustments to the CCIV's membership rights.	
5. As discussed above, a CCIV is entitled to vote on a resolution at a meeting of the members of the sub-fund. What is the appropriate mechanism to facilitate the CCIV's vote?	a) Yes. However, in circumstances where the CCIV does have a conflict of interest in the proposed resolution of a sub-fund in which the CCIV holds shares, we recommend that the voting prohibition should apply to prevent those

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Consultation Questions	KPMG Law Comment
a. Should the corporate director be able to exercise the vote on behalf of CCIV provided it does not have a conflict of interest, and subject to its broader statutory duties to act in the interests of members? b. If the CCIV was the only member of the sub-fund (because, for example, it is a sub-fund in a master-feeder structure), and the corporate director was conflicted from exercising the vote, is another mechanism required to ensure the resolution can be obtained? c. Alternatively, should a mechanism be included in the Regulations that would allow the members of the investing sub-funds to exercise the CCIV's vote? This approach would effectively involve 'tracing through' the CCIV's interest to the interests of the relevant members of the sub-fund.	shares being voted and allow the remaining shareholders in that sub-fund to pass the relevant resolution. b) If the CCIV is the only member of the sub-fund, then there should be an exception to the application of the voting prohibition to enable the CCIV to vote but provided that the vote is cast in the best interests of the sub-fund. c) A "trace through" voting mechanism is not required. One is not required under the current managed investment scheme, nor is it required under the Bill.
6. Are any further adjustments required for any other membership rights the CCIV gains in its capacity as a member of the CCIV and sub-fund under cross-investment?	Where a shareholder vote concerns the whole CCIV, cross-invested shares may need to be disregarded in the vote to avoid double counting.

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Consultation Questions	KPMG Law Comment
Duties of the corporate director of a CCIV Cross-investment may give rise to circumstances where the corporate director, in operating the CCIV, could preference the interests of the members of one sub-fund over the members of another sub-fund of the CCIV.	
7. The corporate director of a retail CCIV is subject to general duties as the director of the CCIV under Part 2D.1 of the Corporations Act, as well as additional duties that are based on those that the responsible entity of a registered scheme owes to members of the scheme under section 1224D of the draft bill. These additional duties prevail over the general duties in the event of a conflict between duties. a. Are these duties appropriate and do they provide equivalent investor protections for members of a CCIV as provided to members of a registered scheme? b. Section 1224D generally sets out duties in respect of the 'members of the CCIV' as whole and not the members of each sub-fund separately – given the CCIV is the overarching collective investment vehicle. Should any additional duties be set out in respect of members of each sub-fund of the CCIV?	Generally, these duties do provide equivalent investor protections to those provided to members of a registered scheme. However there is one scenario where the protections seem to fall short of those currently available to members of a registered scheme; namely the scenario where a company is a RE of two separate registered schemes and wishes to enter into a contract in its capacity as the RE of the first scheme where the contractual counterparty to that contract is the same company in its capacity as the RE of the second scheme. In this scenario, Chapter 5C imposes a conflicts management duty separately on the company in its capacity as RE of each of the two individual schemes. In those circumstances, the corporate RE can only resolve this direct duty-duty conflict by specific conflicts management protocols (e.g. separate teams etc). Under the Bill, the corporate director will not be under the same obligation to manage the conflict in circumstances where the interests of one sub-fund may not be aligned with the interests of another sub-fund.
8. Under the 2019 draft bill, the corporate director of a wholesale CCIV was subject to duties as the director of the CCIV under Part 2D.1 of the Corporations Act but no further duties that are comparable to those owed by a corporate trustee of a wholesale managed	In a wholesale CCIV, the proposed duties would not be appropriate. A wholesale managed investment scheme today which is not a registered scheme is not subject to those proposed duties. It is important to maintain

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Consultation Questions	KPMG Law Comment
investment scheme. Revisions have been made to ensure the corporate director of a wholesale CCIV owes comparable duties to its members – to ensure appropriate investor protections are provided given the facilitation of cross-investment (see section 1224D). These additional duties prevail over the general directors' duties in the event of a conflict between duties. a. Are the proposed duties appropriate and do they provide equivalent protections for members of a wholesale CCIV as provided to members of a wholesale scheme? b. b. Similar considerations arise in respect of the duties owed to 'members of the CCIV' as whole (see Question 7b above). Should any additional duties be set out in respect of members of each sub-fund of the CCIV?	alignment between a wholesale registered scheme and a wholesale CCIV in this regard.
9. Under draft section 1224D(2)(f), the corporate director of a retail CCIV is required to ensure the assets of a sub-fund of the CCIV are valued at regular intervals appropriate to the nature of the assets. This duty is based on an equivalent duty owed by the responsible entity of a registered scheme under section 601FC(1)(j). Treasury is considering whether further requirements should be in place to ensure these valuations are independently reviewed or audited as an integrity measure.	It is not necessary to go further than the equivalent duty owed by the RE under s 601. Such a duty should not be imposed on wholesale CCIVs.

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Consultation Questions	KPMG Law Comment
a. How would such a requirement be implemented in practice? Do any particular considerations need to be taken into account in settling these requirements?	

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