New collective investment vehicles announced in Australia's Federal Budget 2016/17

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In brief

As part of its *ten year enterprise tax plan* announced in last week's Federal Budget, the Federal Government has committed to the introduction of a new tax and regulatory framework for two new types of collective investment vehicles (CIVs) – a corporate CIV and limited partnership CIV. The introduction of these two new vehicles brings Australia more closely into the line with a number of other jurisdictions where these types of vehicles are a fairly common structure for collective investment.

While the formal design and tax treatment of the CIVs is still to be determined in consultation with industry, the new CIV regime is a step in the right direction towards increasing the global competitiveness of Australia's funds management industry, particularly given its alignment with the anticipated commencement of schemes compliant with the Asia Region Funds Passport (the Passport) in 2017.

In detail

Overview of the new CIVs

The Federal Government's 2016/17 budget papers provide for the introduction of two new vehicles to allow investors to pool their funds and have them managed by a professional funds manager. A corporate CIV will be introduced for income years starting on or after 1 July 2017, to be followed by a limited partnership CIV for income years starting on or after 1 July 2018.

The new CIVs will be required to meet the same eligibility requirements as managed investment trusts (MITs), such as being widely held and engaging in primarily passive investment. While MITs are currently the most common form of CIV used in Australia, they are less prevalent in many overseas financial centres and as a result are often avoided by foreign investors who lack understanding of their tax and regulatory framework or may perceive trust structures as an investment vehicle being higher on the risk spectrum.

The introduction of both corporate and limited partnership CIVs, being more common types of investment vehicles that foreign investors generally understand and are more familiar with, removes a natural barrier for foreign investment and increases the attractiveness of inbound investment in Australian managed funds. While this is an obvious motive behind introduction of the new CIVs, it is intended that they not be limited to attracting capital from only foreign investors.

Alignment with commencement of the Passport

Introduction of the new CIV regime from 1 July 2017 is intended to align with commencement of the Passport, with the recently signed Passport Memorandum of Cooperation ("MOC") between Australia, Japan, Korea and New Zealand expecting to result in the first Passport-compliant schemes being offered by participating economies in 2017.

The Passport is an international initiative that seeks to create a common framework to reduce regulatory inconsistency and overlap faced by collective investment scheme operators offering schemes in multiple jurisdictions. This facilitates the cross-border offering of eligible collective investment schemes while ensuring investor protection in participating jurisdictions. For further information on the Passport, please refer to our publication *Asian Passports, the coming of age*.

Introduction of the new CIVs will inherently improve the effectiveness of the Passport from an Australian perspective by allowing Australian fund managers to offer a broader range of CIVs, particularly those that foreign investors may be more familiar with. With USD 4.5 trillion assets under management as at June 2015, the Asian Region is an important growth area for funds management and one that Australian funds can get better exposure to following commencement of the new CIV regime in conjunction with the Passport.

Expected form and tax treatment

The formal design of the new CIVs has not yet been determined and is expected to require detailed consultation between Treasury and industry to develop, particularly in light of current corporations and partnership laws. The draft Passport rules also require detailed consideration and possible amendment to ensure the new CIVs are not excluded from the concept of a 'collective investment scheme'. It is worth noting that the current statutory regime for publicly offered investments in Australia does not provide for the operation of certain alternative forms of collective investment vehicles that are common in overseas jurisdictions such as UCITS)Undertaking for Collective Investment in Transferable Securities) funds that currently operate under the EU directive. A UCITS investment structure cannot be registered as a managed investment scheme under the Corporations Act, as the UCITS structure does not include the equivalent of the single responsible entity. Additionally, the UCITS Directive constitutes a prescriptive regulatory regime, where structural requirements for a UCITS are embedded in a law for a UCITS. Essentially, the managed investment scheme and current corporations regime for public offers in the Corporations Act does not contain equivalent requirements.

Similar to the existing MIT structure, it is expected that both the corporate and limited partnership CIVs' will have flow through status for tax purposes, meaning investors will generally be taxed as if they had invested directly. However, the specific tax attributes of the new CIVs will also need to be determined in consultation with industry, specifically with respect to the application of Australia's withholding tax rules to the CIVs.

Practical outcome for Australia's funds management industry

As noted above, introduction of the new CIV regime should enhance access by the Australian funds industry to foreign markets and allow more product choice by enabling Australian fund managers to offer a broader range of CIVs and thereby eliminate a natural barrier for inbound investment into Australia. In line with the broad intention of the Federal Government's *ten year enterprise tax plan*, this is expected to increase the global competitiveness of Australia's fund management industry and lead to the realisation of greater commercial success of the Passport from an Australian perspective.

In addition to increasing competitiveness of the Australian funds industry, the new CIV regime also provides an opportunity for Australia to pursue and lead innovation in the financial sector. In response to the Financial System Inquiry conducted in late 2013, the Federal Government cited the Passport as one of three opportunities for innovation in the financial sector. The Assistant Treasurer's announcement of signing of the MOC also noted the Passport as one of the latest innovative measure in funds management. While the new CIVs provide a crucial means by which Australia can realise success of the Passport, it is expected that new ways of connecting the users and savers of capital will emerge beyond the current MITs and proposed CIVs. This presents an opportunity for Australia to lead innovation in funds management; by not only striving to meet global competition but pushing the boundaries to redefine what CIVs of the future might look like.

Let's talk

For a deeper discussion of how these issues might affect your business, please contact:

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