Level 2
95 Pitt Street Sydney, NSW 2000
Telephone 02 8223 0000
Facsimile 02 8223 0077
Email tia@taxinstitute.com.au
Website www.taxinstitute.com.au
ABN 45 008 392 372

TAXATION INSTITUTE of AUSTRALIA
IT'S ESSENTIAL

8 January 2010

The General Manager
Business Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

Email SBTR@treasury.gov.au

Dear Sir/Madam

MANAGED INVESTMENT TRUSTS – CAPITAL GAINS TAX ELECTION

The Taxation Institute of Australia (**Taxation Institute**) is pleased to provide comments on the exposure draft (**ED**) and explanatory material (**EM**) in relation to the election to allow capital gains tax to be the primary code for certain disposals by managed investment trusts.

The Taxation Institute welcomes the proposal to allow managed investment trusts (**MITs**) to make an election to treat gains and losses on disposal of certain investments on capital account for taxation purposes.

The Taxation Institute's comments in relation to the ED and EM are set out below.

1. Eligible Australian MIT

Only eligible MITs will be able to make an irrevocable election to apply the CGT regime to all eligible disposals (**CGT Election**).

The eligibility status of a MIT will be determined on a year by year basis. This may create significant compliance issues. For example, gains and losses will need to be tracked and attributed to periods when the MIT was or was not an eligible MIT.

The Taxation Institute recommends that the CGT Election be structured as a "once and for all election". That is, if a MIT is eligible and makes the CGT Election, the election will remain in force even if the MIT no longer satisfies the criteria to be an eligible MIT. The Taxation Institute considers that this approach would effectively deal with the compliance costs and the integrity issues associated with MITs manipulating the CGT Election (ie by coming in and out of the regime depending on which approach is more beneficial).

Generally, to be an eligible MIT, the trust must be operated by a financial services licensee (ie unless a licence is not required because the trust is operated by a Crown entity or a person with an ASIC exemption).

The Taxation Institute considers that the status of certain unregistered managed investment schemes and the treatment of the different kinds of financial services licences that can be issued remains uncertain under the ED. Further, the ED does not address the common situation of a licence held by a person other than the trustee where the trustee is simply an authorised user of the licence. The Taxation Institute submits that these issues need to be specifically dealt with in the ED or EM.

Further, the Taxation Institute considers that it would be inappropriate to exclude unregistered schemes as this would exclude many wholesale funds, which clearly should be within the scope of the measures. The Taxation Institute notes that subsection 275-5(4) appears to be designed to deal with this issue. However, as that subsection requires "every" member of a trust to be a MIT to satisfy the conditions of the subsection, there will still be some wholesale funds that are excluded.

The Taxation Institute also considers that the EM should provide some more specific examples in relation to the eligibility status of MITs. In this regard, examples could be provided to illustrate the application of the provisions to wholesale funds and to funds which have non-resident investors.

On a broader level, the Taxation Institute considers that further consideration should be given to expanding the CGT Election to other collective investment vehicles not just MITs excluding superannuation funds which already have deemed capital treatment (eg listed investment companies and venture capital limited partnerships) and those trusts that are subject to regulatory regimes other than the Corporations Act (eg those regulated by the superannuation and life insurance regimes).

2. Eligible disposals

The ED provides that capital treatment can be elected where the disposal of the eligible asset constitutes a CGT event arising from the disposal or other realisation of the asset for the purposes of the CGT provisions.

It appears that this is intended to further limit the scope of the CGT Election. If it is intended as a further limitation, this may mean that the capital/revenue characterisation of gains and losses in relation to certain transactions which relate to those assets and give rise to a CGT event under the CGT regime which is not strictly a "disposal or other realisation" of the asset will remain an issue (eg premiums received on the grant of a lease, payments for entering restrictive covenants, amounts received for granting an option over an asset and payments where the underlying share or units remain on issue such as a reduction of capital).

The Taxation Institute considers that the concept of an "eligible disposal" should be expanded to an "eligible event" which should include all CGT events and, if appropriate, certain CGT events can be carved out. This would be consistent with the approach in the superannuation rules (refer s 295-85 of the *Income Tax Assessment Act 1997*).

3. Transitional issues

The EM should specify what happens where a MIT has already made their 2009 distributions before the enactment of this legislation and the ability to make a CGT Election. That is, for the avoidance of doubt, the EM should specify whether such MITs will be required to amend their classifications. For example, the EM should specify the correct practice where a MIT has classified certain losses as revenue losses and has then used these losses to offset certain revenue gains prior to making the CGT Election which will result in the revenue losses being classified as capital losses and being unable to be offset against the revenue gains.

4. Other comments

Subsection 275-5(7) excludes any trust which is closely held at any time during an income year. When a MIT is in its early formation stages, the MIT may be a closely held trust but may comply soon after its formation time. The Taxation Institute considers that subsection 275-5(6) should extend to cover such circumstances. However, as currently drafted, subsection 275-5(7) appears to be outside the scope of subsection 275-5(6).

There is an omission in subsection 275-5(8) in the first line, the reference to subparagraph (c)(ii) should be to (1)(c)(ii).

The Taxation Institute considers that it is unclear why subsection 275-17(2) is confined in its operation to paragraph 275-17(1)(b) and does not apply to paragraph 275-17(1)(a). The reason should be explained in the EM or the section should be re-drafted.

Lastly, the Taxation Institute considers that the word “gain” in subsection 275-100(2) requires clarification.

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If you require any further information or assistance in respect of our submission, please contact David Williams on 02 9958 5121 or the Taxation Institute’s Tax Counsel, Angie Ananda, on 02 8223 0011.

Yours sincerely

David Williams
President