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PARTNERSHIPS
AUSTRALIA

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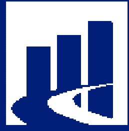
SUBMISSION:

The review of tax arrangements applying to collective investment vehicles

MARCH 2011

Infrastructure Partnerships Australia is a national forum, comprising public and private sector CEO Members, advocating the public policy interests of Australia's infrastructure industry.



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ABOUT INFRASTRUCTURE PARTNERSHIPS AUSTRALIA

Infrastructure Partnerships Australia is the nation's peak infrastructure body. Our mission is to advocate the best solutions to Australia's infrastructure challenges, equipping the nation with the assets and services we need to secure enduring and strong economic growth and importantly, to meet national social objectives.

Infrastructure is about more than balance sheets and building sites. Infrastructure is the key to how Australia does business, how we meet the needs of a prosperous economy and growing population and how we sustain a cohesive and inclusive society.

Infrastructure Partnerships Australia seeks to ensure governments have the maximum choice of options to procure key infrastructure. We believe that the use of public or private finance should be assessed on a case-by-case basis.

IPA also recognises the enhanced innovation and cost discipline that private sector project management and finance can deliver, especially with large and complex projects.

Our Membership is comprised of the most senior industry leaders across the spectrum of the infrastructure sector, including financiers, constructors, operators and advisors. Importantly, a significant portion of our Membership is comprised of government agencies.

Infrastructure Partnerships Australia draws together the public and private sectors in a genuine partnership to debate the policies and priority projects that will build Australia for the challenges ahead.

INTRODUCTION

Infrastructure Partnerships Australia (IPA) is pleased to provide this submission in response to the Board of Taxation's discussion paper: *Review of tax arrangements applying to collective investment vehicles (CIVs)*.

A January 2010 report of the Australian Financial Centre Forum, *Australia as a Financial Centre – Building on Our Strengths* (the Johnson Report) recommended 'that the Treasurer request the Board of Taxation to review the scope for providing a broader range of tax flow through collective investment vehicles.'[1] The current review arises from that recommendation. The Board has been asked to examine and report on the tax treatment of CIVs, with regard to the managed investment trust (MIT) tax framework and considering whether a broader range of tax flow-through CIVs should be permitted.

IPA supports expanding the range of CIVs with flow-trough tax treatment. Such measures would improve Australia's international competitiveness in attracting funds under management and enhance Australia's status as a leading regional financial centre.

A 2010 OECD report states that just under US$20 trillion is invested through CIVs globally.[2] Australia had $1,351 billion in collective investment funds under management at the end of June 2010. However, only 5 per cent of those funds come from overseas investors.[3]

The Johnson Report found that certain features of Australia's tax and regulatory frameworks applying to the funds management sector place the sector at a competitive disadvantage in terms of managing funds for overseas clients. The Report also found that this could be improved if Australia had a broader range of appropriate investment vehicles to sell into Asia, which were taxed on a flow-through basis.

The levels of investment needed for the development of essential new infrastructure in Australia far exceed what government can provide.[4] Resolving this shortfall will require the development and implementation of frameworks that efficiently harness additional private sector capital, including from offshore investors. Policymakers have a role to play in establishing the appropriate tax and regulatory frameworks to encourage overseas investment in domestic infrastructure assets. Any Australian CIV regime would benefit greatly from adopting attributes that encourage global investors; and infrastructure investment would benefit greatly by being included in that CIV regime.

[1] The Johnson Report, Recommendation 3.3.
[2] The Granting of Treaty Benefits with respect to the Income of Collective Investment Vehicles (OECD April 2010).
[3] Managed Funds, Australian Bureau of Statistics (ABS) June quarter 2010.
[4] A 2008 report released by ABN Amro, as it then was, quantified Australia's infrastructure investment task at $455 billion (in 2007 terms) over the next decade. A 2008 Citigroup study estimated that this figure was a les conservative $770 billion (again in 2007 terms) over the decade. A 2010 ANZ study reported that $600 billion would be needed in infrastructure investment in the following six years.

IPA presents this submission with a focus on those of the issues the Board is seeking comment on relevant to the infrastructure industry. Those are:

- Impediments to foreign investment through CIVs
- CIVs for the purposes of this review
- The Limited Partnership (LP) regime
- Creating a new corporate CIV regime

IMPEDIMENTS TO INVESTMENT INTO AUSTRALIA BY FOREIGN INVESTORS THROUGH CIVs

Q 2.1 Issues/Questions

The Board seeks stakeholder comments on:

- the specific reasons for the apparent unattractiveness of Australia's current tax treatment of CIVs to non-resident investors;

IPA supports the extension of flow-through taxation treatment to widely held entities other than trusts. IPA believes that flexibility of choice of investment vehicle should enhance the ability of Australia to attract foreign capital in infrastructure projects.

Australian infrastructure projects are often structured using a flow-through vehicle (CIV Trust) and a stapled operating company (see for example Figure 1 below, and the explanation for the use of such structures).

There are a number of offshore jurisdictions that are not familiar with the concept of trusts (particularly European countries). Difficult questions of characterisation of trust distributions can arise for such investors in their home jurisdictions. Tax provisions are typically focussed on the receipt of dividends on shares and hence trust distributions are not easily catered for under many foreign laws. This uncertainty of outcome can lead to higher costs of capital for an Australian investment, or discourage investment.

Giving foreign investors the flexibility of choice of Australian look-through vehicles to manage their domestic tax, regulatory and commercial positions, without prejudice to the Australian revenue, is supported by IPA.

Q 2.1 Issues/Questions (cont.)

The Board seeks stakeholder comments on:

- the specific non-tax factors which may make Australia's CIVs unattractive to non-resident investors.

As stated above, there is a lack of familiarity with trusts in non-common law jurisdictions, and the proliferation of trusts in Australia may deter investors from those jurisdictions.

CIVs FOR THE PURPOSES OF THIS REVIEW

Q 2.2 Issues/Questions

The Board seeks stakeholder comments on:

- the appropriateness of the widely held definition contained in the MIT legislation as a characteristic for a wider range of CIVs, and whether there are any compelling reasons to have non-widely held vehicles included as CIVs;

IPA is supportive of an approach whereby similar concepts of widely held are applied to look through trust CIVs (MITs) and non-trust CIVs.

Clearly the MIT rule definitions will need to be refined because the differing concepts of registered and unregistered managed investment schemes are not relevant for limited partnerships or companies.

IPA also notes member concerns that there are a number of anomalies and uncertainties contained within the MIT rules as recently amended, particularly in the area of tracing of MIT participation interests. Close adoption of new widely held rules for companies and limited partnerships would therefore require extensive consultation.

Q 2.2 Issues/Questions (cont.)

The Board seeks stakeholder comments on:

- the appropriateness of the current definition of eligible investment business in Division 6C of the ITAA 1936 as a prerequisite for a wider range of CIVs, and whether there are any compelling reasons why vehicles undertaking investment activities involving control of active businesses should be included as CIVs

IPA supports the proposition that the eligible investment business requirements apply in the same way for CIV Trusts, or other CIV entities. However, as explained below, IPA believes the eligible investment business requirements should be revisited for CIV trusts and other CIV entities.

Eligible Investment Business

To retain its flow-through taxation treatment and not be taxed as a company, a CIV Trust (that is a public unit trust) must not be a trading trust as defined in section 102N of the ITAA 1936. This means that the CIV Trust must not either (i) carry on a trading business or (ii) control another person in respect of the carrying on by that other person of a trading business. Thus the activities

of the CIV Trust (or of any person controlled by the CIV Trust) must be restricted to "eligible investment business", so that a trading business is not carried on.

Secondly, eligible investment business is also important for the application to MITs. To retain concessional withholding treatment and deemed capital treatment otherwise available to a CIV Trust that is a MIT, the CIV Trust must not carry on a trading business.

Relevantly to this submission, eligible investment business is defined restrictively in the context of infrastructure projects to include:

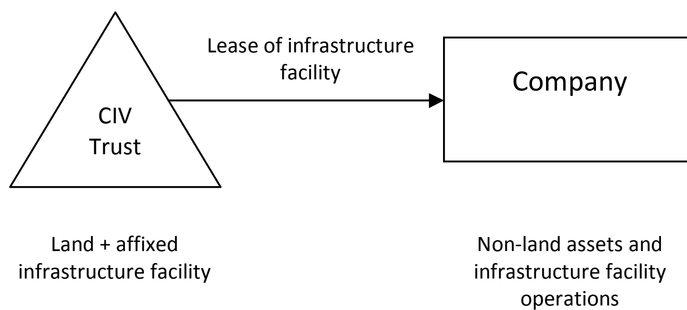
"investing in land for the purpose or primarily for the purpose of deriving rent".

IPA has made a number of submissions to Treasury in recent years in relation to this issue. The crux of the submissions has been that the definition is too restrictive to encompass the variety of ways in which income is derived from the exploitation of an infrastructure facility. Examples of non-rental income derived from the exploitation of an infrastructure facility that do not amount to rent would include:

- toll roads producing tolls
- ports producing income not being rental income simpliciter e.g. wharfage, harbour dues
- social infrastructure projects (such as schools, hospitals and prisons) producing an availability payment that includes a services component
- gas pipelines producing income from the transportation of gas (i.e. a service)
- power generation assets producing electricity for sale (i.e. a product)

As a result of the restrictive definition of eligible investment business within Division 6C, the market practice has been to separate an infrastructure into two parts. The first being the eligible investment business activities including the leasing of the land component of the infrastructure project to derive rental income. The second being the active business/trading activities which have been conducted in a company. A typical stapled trust/company structure is shown diagrammatically at Figure 1.

Figure 1 – Stapled Structure

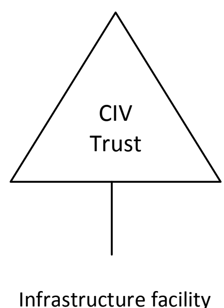


Ideally IPA members would like to see infrastructure facilities treated as real property and brought into the broad property exclusions, with a specific Division 6C carve-out for infrastructure project investments.

IPA proposes that all infrastructure activity should have its own paragraph in relation to being an eligible investment business activity for tax purposes. Alternatively, this could be done by adding to the definition of "investment in land" as "including infrastructure facilities" and then listing out such infrastructure. As a starting point, infrastructure facilities should be defined to include, but not be limited to, those facilities covered by the definition of infrastructure facilities in section 93L of the *Development Allowance Authority Act 1992*. IPA would wish to be consulted in relation to further inclusions to ensure the definition is adequate.

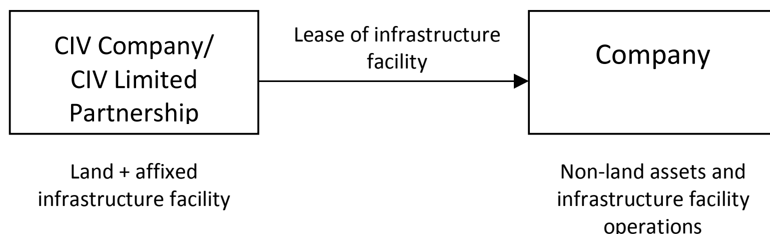
IPA believes that the inclusion of income derived from an infrastructure facility as eligible investment business would obviate the need for stapled structures in an infrastructure context. This would substantially reduce the complexity for both non-resident and resident investors. A simplified structure is shown below as Figure 2.

Figure 2 – Infrastructure Facility with eligible Investment business (including in respect of an infrastructure facility)



In the event that the definition of eligible investment business is retained as currently drafted for a CIV Trust or a CIV Company/other entity, this separation process of eligible and non-eligible activities will practically continue. That is, if a look-through company or look-through limited partnership is permitted under the CIV reforms, and the activities of those entities are restricted to eligible investment business activities as currently drafted then the stapling of a separate company with the active business activities to the CIV look-through entity will continue (see figure 3 as an example).

Figure 3 – Stapled CIV

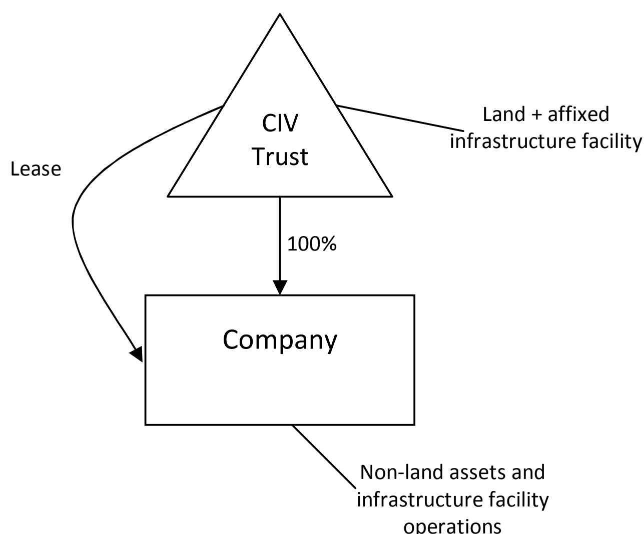


Allowing a controlled company to be owned by a CIV Trust/CIV entity

From a high level policy perspective, IPA submits that if trading income is clearly subjected to the company tax system and company tax is paid, then there should be no requirement for the investment fund which happens to control such a company to be disentitled from the ability to flow-through dividend income and to conduct its own eligible activities.

Figure 4 shows the simplification that could be achieved for infrastructure vehicles in the event that a controlled company is permitted to be owned by a CIV Trust.

Figure 4 – Controlled Company Structure

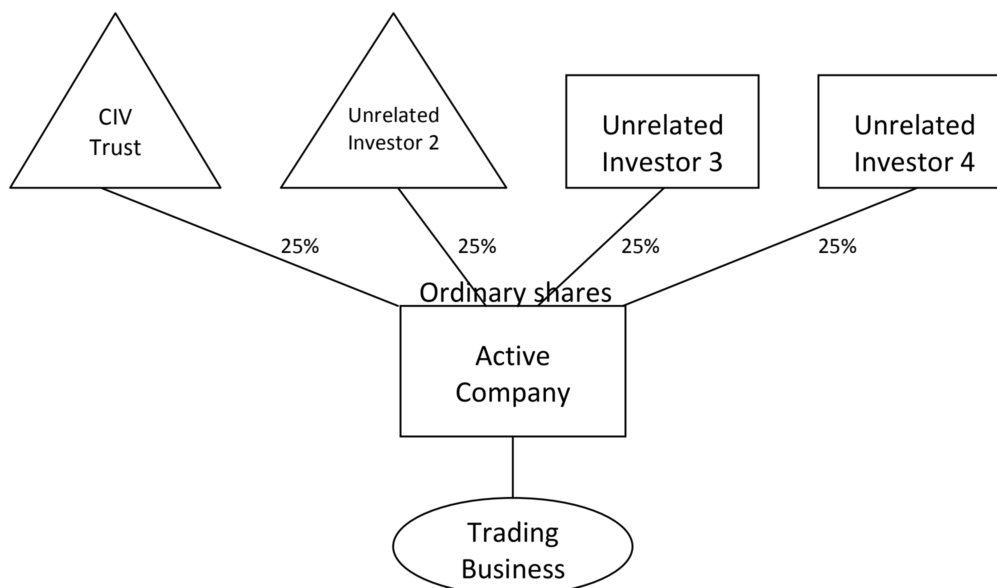


Q 2.2 Issues/Questions
The Board seeks stakeholder comments on:
• whether there is a need to further define 'control' in Division 6C of the ITAA 1936 to provide greater certainty for investors in MITs and other CIVs, and if so, how this could be achieved.

As discussed above, IPA does not believe that the mere control of a company should make a CIV Trust a trading trust. In the event that the concept of control is retained, IPA believes that the concept of control should be defined as "positive" control, rather than negative control through veto power. IPA believes that this would make it clearer that is what it is intended.

IPA would particularly like to refer to the Private Binding Ruling 1011493321924 released in October 2010 and ATO Interpretative Decision ATO ID 2011/11 released on 18 February 2011. This is shown in Figure 5 below.

Figure 5



The facts are that a CIV Trust held a 25% interest in a company that carried on an active business. Three non-related investors held a 25% interest each in that Company. The investors in the company had entered into an agreement (Shareholders Agreement) that effectively gave investors a blocking or veto right in respect of a list of Shareholder Reserved Matters above a threshold level of ownership. A vote on any Shareholder Reserved Matter required an 80% vote to be passed. Examples of Shareholder Reserved Matters could be:

- sale of a business undertaking by the company
- incurrence of capital expenditure above a certain threshold
- refinancing of debt
- change of CEO
- other matters.

The ATO ID indicated that the investor CIV Trust or any other investor with a blocking stake (a shareholding above the threshold percentage) would “control” the affairs or operations of the company based upon the relevant facts, notwithstanding that the investor had no positive control over the company.

This ruling is illustrative of the difficulty that can exist in interpreting what will amount to control of the affairs or operations of a company, particularly if negative control or restraint is sufficient to amount to control. An extract from the ruling showing the difficulties that can arise is as follows:

"The word "control" is not defined for the purposes of Division 6C and accordingly, as acknowledged by the High Court, must be construed by reference to its natural meaning refined by its context.

The courts have held that the word "control" is a slippery concept and has a number of possible meanings. The Australian Oxford Dictionary defines the word "control" as (i) the power of directing, command; (ii) the power of restraining, especially self-restraint; and (iii) a means of restraint; a check. Plainly, the concept of exercising control includes both the positive aspect of directing or commanding and the negative aspect of restraining.

Whereas one might ordinarily reflect on control of a company in terms of its Board of Directors ultimately answerable to a majority vote by shareholders, it is a perspective which does not accommodate the notion of negative control and, in turn, would narrow the scope intended by Parliament for the operation of paragraph 102N(1)(b) of the ITAA 1936. The language of the provision and its supporting materials make clear that the legislative intention did not proceed on the myopic footing that control can be exercised only through a majority vote of shareholders.

In Re The News Corporation Ltd and Others, the concept of control in the context of the Broadcasting and Television Act 1942 was given wide import. In that case, Bowen CJ held that a "power of veto is a power to restrain, and hence to control". The statement by Bowen CJ was made and meant, on its face and in its context, as a statement of general principle.

In the present case, the trustee of the MIT (through its voting power) can block a resolution put to the shareholders by the Board of Directors. In other words, irrespective of the status of any other shareholder in OpCo, any matter listed as a Shareholder Reserved Matter is blocked if the trustee of the MIT exercises its power of veto, i.e. negative "control"."

A voting threshold over Shareholder Reserved Matters is often set in shareholder agreements dealing with consortium acquisitions of infrastructure assets. This is so that minority shareholders have comfort that the company cannot undertake certain actions that are not consistent with the business case upon which the investor initially committed their investment. The IPA is very concerned that CIV Trusts that take minority stakes in companies could be viewed as having negative control and on one view control of the affairs or operations of the company even though those shareholdings could be relatively small e.g. less than 20%. This would make the CIV Trust a trading trust. IPA does not believe this is the way that control was intended to be interpreted and it creates extreme uncertainty.

Using the ATO ID 2011/11 logic, all four non-related investors could effectively "control" the affairs or operations of the company. This is obviously an extraordinary result. The ATO ID leaves many CIV Trusts questioning their ability to have a veto over shareholder matters and to question which shareholder matters may be acceptable and those that go to control.

IPA believes that the test of control could be governed in a similar way to that proposed in the proposed new CFC rules released on 17 February 2011. That is a definition of control based upon Australian Accounting Standard AASB 127 as “the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities”.

LIMITED PARTNERSHIPS (LPs)

Q 3.3 Issues/Questions

The Board seeks stakeholder comments on:

- generally, what changes could be made to the LP regime to provide for an appropriate LP CIV;

IPA submits that the LP regime should generally be based on the current partnership provisions contained in Division 5 of the *Income Tax Assessment Act 1936* (ITAA 1936) with a number of restrictions or integrity provisions which would align this regime to similar regimes overseas.

IPA submits that the LP CIV regime would require the following features so that it is aligned to similar overseas regimes (for example, in US, UK, Ireland, NZ, etc):

- As per our current partnership regime, income and losses of the LP CIV should be attributed to the partner.
- An eligible LP CIV could be excluded from the operation of Division 5A (Income of certain Limited Partnerships) by a specific exception in section 94D(2).
- The Explanatory Memorandum (EM) accompanying the *Taxation Laws Amendment Act (No. 6) 1992* which enacted Division 5A of the ITAA 1936 noted that if limited partners were treated in the same way as partners in any other partnership, the limited partners may benefit from distributions of losses that exceed their limited liability.
- The EM further provided and as noted at paragraph 3.42 of the Discussion Paper that these losses could be used by the limited partner to reduce their taxable income even if the limited partner was not exposed to any risk of having to meet obligations or make good on those losses.
- In order to address this issue, IPA submits that a restriction could be included in the current partnership regime that a limited partner's entitlement to losses is limited by its total contribution of capital. Note that a similar restriction is included in other jurisdictions (for example, the UK - refer to section 104 Income Tax Act 2007 (UK) and sections 117 and 118 of the Income and Corporation Taxes Act 1988 (UK); NZ - refer to section HG 11(3) of the Income Tax Act 2007 (NZ); HK - refer to section 22B(3) Inland Revenue Ordinance (No 112)).

Q 3.3 Issues/Questions (cont.)

The Board seeks stakeholder comments on:

- whether LPs are suitable vehicles for widely held, primarily passive and collective investments;

IPA submits that LPs are suitable vehicles for collective investments for the following reasons:

- In a speech given by the Assistant Treasurer, The Hon Bill Shorten MP, at an Australian Chamber of Commerce gathering in Hong Kong on 19 January 2011, he stated that Australia is in the process of creating a 'level playing field' in respect of financial services, particularly funds management (including effectively funds management special purpose vehicles).

- One of the main reasons for introducing a LP CIV regime in Australia is that it would create such a 'level playing field' (that is, a more competitive environment to attract global business and promote specialist financial services) for both Australian managed funds and Australian investments as compared to the rest of the world.

- The LP regime is well recognised and utilized both in Australia and overseas. In contrast, the trust regime is not as well understood/recognised overseas - particularly in civil law countries. This creates a hurdle for Australian investment offerings to attract offshore investment as the use of trusts is prevalent in Australia due to the benefits associated with its structure such as the recent managed trust investment withholding tax concession and the capital account election. However, certain offshore investors can be hesitant to invest into trusts as they are structures that they are not as familiar with or recognise/understand.

On this basis, an expansion of the current LP regime would be well received and understood/recognised by potential investors both in Australia and overseas and create greater flexibility and options for fund raising vehicles, particular special purpose vehicles.

IPA submits that, for the reasons discussed above, Australia would see increased investments from domestic and offshore investors if an appropriate LP CIV regime were introduced; including potentially investments and investors using Australia as a conduit for offshore investment.

We submit that the LP CIV regime should not be restricted to widely held and primarily passive requirements for the reasons discussed below; particularly to attract a greater range of wholesale investors.

Q 3.3 Issues/Questions (cont.)

The Board seeks stakeholder comments on:

- Whether it is desirable to introduce changes to the LP regime, so that flow-through taxation is allowed for those widely held LPs that restrict their investment activities to primarily passive investments;

IPA submits that it would be highly desirable to introduce changes to the current LP regime so that flow-through taxation is allowed to make Australia more competitive and attractive to foreign investors and funds from a commercial perspective.

However, to introduce flow-through taxation only for widely held LPs that restrict their investment activities to primarily passive investments would put Australia in a disadvantageous position to other jurisdictions that do not contain such prescriptive restrictions. For example, in the UK - the LP cannot consist of more than 20 persons and must consist of one or more partners called general partners (refer to section 4 of the Limited Partnership Act 1907 (UK)). Further, there is no restriction in the UK for the LP to have primarily passive investments. Also, in China - the LP should have more than 2 but less than 50 partners with at least one 'common partner' (that is, general partner) (refer to article 61 of the Partnership Enterprise Law). In this context, the Australian trust equivalent of Division 6C is overly restrictive and outdated in view of more recent developments to tax superannuation funds and with the broader and more sophisticated range of asset classes to seed and / or attract managed funds.

IPA submits that to restrict the LP CIV regime to primarily passive investments would not be as attractive for large infrastructure projects (such as power stations, desalination plants and ports) in Australia to be funded by foreign investors as the nature of these projects is not exclusively passive.

Q 3.3 Issues/Questions (cont.)

The Board seeks stakeholder comments on:

- If flow-through were allowed for LPs marketed at the wholesale level or for sophisticated investors that restrict their investment activities to primarily passive investments, would it be appropriate not to require these LPs to be ‘widely held’ (as defined in the MIT regime)? What would be the rationale for allowing this when compared to MITs which are required to be widely held;

IPA submits that it would not be appropriate to require LPs to be 'widely held' where the LPs are marketed at the wholesale level or for sophisticated investors. The rationale would be to align the Australian LPs to similar overseas regimes as discussed above.

However, if a 'widely held' requirement was contained in the modified LP CIV regime, IPA submits that this should be similar to that contained in the MIT regime which allows tracing through various entities and concessionary rules in respect of foreign collective investment vehicles and sovereign funds.

Q 3.3 Issues/Questions (cont.)

The Board seeks stakeholder comments on:

- Apart from limiting the flow-through of losses, would there be a need, in light of integrity and investor protection considerations, to apply further restrictions to that modified LP regime? If so, what would be the nature of those restrictions;

IPA submits that the following integrity measures which are utilised overseas could also be used as a model / precedent in any modified Australian LP regime:

- A limited partner shall not take part in the management of the partnership business, and shall not have power to bind the limited partnership (refer to section 6(1) of the *Limited Partnership Act 1907* (UK)).

- A person cannot be both a general partner and a limited partner of the same limited partnership at the same time (refer to section 8(2) of the *Limited Partnership Act 2008* (NZ)).

- A distribution can only be made provided the LP satisfies the solvency test (refer to sections 39-45 of the *Limited Partnership Act 2008* (NZ)).

IPA strongly supports the pass through of losses under the proposed new LP CIV regime particularly as with large greenfields infrastructure projects the losses generating period can last for several years in the start up phase of the relevant projects. The full life cycle (profitable and loss generating) should be recognised for tax purposes in respect of these projects.

A summary of similar LP regimes in the UK, Ireland, US, China, HK and NZ is attached for your reference and guidance (Appendix A).

DESIGN OF A NEW CORPORATE CIV REGIME

Q 4.1 Issues/Questions

The Board seeks stakeholder comments on:

- The appropriateness of any of the taxation models (including variants) to achieve tax neutrality for designing a corporate CIV regime that would enhance industry's ability to attract funds under management in Australia;

IPA submits that the option of flow-through taxation for corporate CIVs is the optimal model to achieve tax neutrality for investment into infrastructure projects in Australia. IPA submits that the flow-through taxation model should have the following features:

- Allow for the flow through of tax losses to shareholders in a manner consistent with Division 5 of the Income Tax Assessment Act 1936 ("1936 Act") with appropriate integrity provisions to the extent necessary to prevent participants benefiting from tax losses in excess of their economic loss plus the amount of any concessional deductions.
- Provide for full attribution of income to shareholders in a manner consistent with Division 5 of the 1936 Act.
- Provide for character flow through in a manner consistent with Division 5 of the 1936 Act.
- Allow for default capital gains tax treatment of gains for shareholders through an irrevocable election.
- Provide for statutory revenue treatment of carry.

Q 4.1 Issues/Questions (cont.)

The Board seeks stakeholder comments on:

- The appropriateness of any of the models (including variants) to achieve tax neutrality for designing a limited partnership CIV regime that would enhance industry's ability to attract funds under management in Australia;

IPA supports the adoption of a tax flow-through model for the taxation of limited partnership CIVs. Further submissions on this point have been made in response to Question 3.3 above.

Q 4.1 Issues/Questions (cont.)

The Board seeks stakeholder comments on:

- Whether there are any critical design features that would improve certainty and simplicity and enable better harmonisation, consistency and coherence across the various CIV regimes including by rationalisation of the regimes where possible;

IPA supports the principles of simplicity, consistency and coherence across the various CIV regimes. However, IPA would be concerned if some of the more onerous eligibility requirements present in the current MIT regime where imported into either the limited partnership CIV or corporate CIV regimes.

IPA notes that a trust must meet a wide range of requirements to qualify as a managed investment trust for the purposes of section 12-400 of the *Tax Administration Act 1953.* In particular, the trust must not carry on or control a trading business, be genuinely widely held and meet certain regulatory requirements.

IPA has made submissions regarding the critical design features of a limited partnership CIV in our responses to question 3.3 above.

IPA submits that the following critical design features should be present in any corporate CIV regime:

- No eligible investment business test requirement. However, if a Division 6C style eligible investment business test is required, ensure that there is a carve out for infrastructure investments consistent with the submissions made in response to Question 2.2 above.

- If a widely held test is required, ensure that the test allows tracing through various types of entities (not merely trusts) and provides concessional rules for investments held by so called "white list investors" set out in section 12-402(3) of the *Tax Administration Act 1953*.

- Flow through tax treatment should be available through the making of an irrevocable election.

Q 4.2 Issues/Questions

The Board seeks stakeholder comments on:

- What would be the most appropriate method to achieve an outcome similar to tax flow through for a corporate CIV;

IPA reiterates that full tax flow through for corporate CIVs available through an irrevocable election is the optimal model to achieve tax neutrality for investment into infrastructure projects in Australia.

However, if full tax flow through is not available, IPA submits that a corporate CIV should be entitled to MIT treatment through an irrevocable election and subject to meeting any applicable widely held and eligible investment business requirements.

Q 4.2 Issues/Questions (cont.)

The Board seeks stakeholder comments on:

- What would be the most appropriate method to determine the tax liabilities of investors in a corporate CIV;

IPA submits that the flow-through taxation model should have the following features:

- Allow for the flow through of tax losses to shareholders in a manner consistent with Division 5 of 1936 Act up to total paid up capital (with appropriate integrity provisions to prevent loss streaming).
- Provide for full attribution of income to shareholders in a manner consistent with Division 5 of the 1936 Act.
- Provide for character flow through in a manner consistent with Division 5 of the 1936 Act.
- Allow for default capital gains tax treatment of gains for shareholders through an irrevocable election.
- Provide for statutory revenue treatment of carry.

IPA submits that where the corporate CIV making the flow through election is instead deemed to be a MIT, the tax liabilities of investors should be determined in accordance with the MIT regime.

Q 4.2 Issues/Questions (cont.)

The Board seeks stakeholder comments on:

- Under what circumstances would it be appropriate to assess tax on a corporate CIV, at what rate, and what should be the tax consequences of the payment of the tax for investors;

IPA submits that the corporate CIV would not be subject to tax where the full flow through model is adopted.

Where the corporate CIV is instead deemed to be a MIT, the company should be subject to tax in the capacity of a notional trustee of the MIT.

Q 4.2 Issues/Questions (cont.)

The Board seeks stakeholder comments on:

- What special rules would be necessary to mesh the corporate CIV appropriately with the rest of the Australian tax system.

No comment

Q 4.2 Issues/Questions (cont.)

The Board seeks stakeholder comments on:

- Would it be appropriate to extend the MIT regime to a corporate entity, by deeming qualifying entities to be trusts for tax purposes? What modifications would be required for corporate entities under such a regime, and would this be feasible without adding undue complexity to the tax and company law?

As noted above, in the absence of a full tax flow through model for corporate CIVs, IPA supports the extension of the MIT regime to corporate CIVs which make an irrevocable election and satisfy any applicable widely held or eligible investment business.

APPENDIX A: COMPARATIVE TABLE OF INTERNATIONAL LP REGIMES

Country	How is income attributed to the LP partners? How are losses treated?	General requirements of a LP	Restrictions of a LP	Benefits of a LP
England and Wales[1] *Limited Partnerships Act 1907 (UK) (LPA)*	All partnerships are tax transparent. Though income tax should be computed and stated jointly and be separate and distinct from any other tax chargeable on the partners.[2] Each individual and corporate partner should be taxed on its respective share of the profits and losses and entitled to relief from income tax in accordance with their respective share in the LP.[3] A limited partner's entitlement to losses is limited by its total contribution of capital.[4]	A LP must be registered in accordance with the Act (in London or Edinburgh, wherever it conducts business), otherwise it is treated as a general partnership.[5] There must be at least one general partner and one limited partner but no more than 20 partners.[6]	It is not a separate legal entity.[7] A limited partner cannot take part in the management of the partnership business and has no power to bind the firm. (Though a limited partner may inspect the books and examine the state and prospects of business and may advise thereon.) Otherwise the limited partner would lose its limited liability.[8] A limited partner cannot draw out or receive back any of its contribution during the partnership.[9]	A limited partner is liable only to the extent of capital contributed at the time of entering the partnership.[10]
Scotland *Limited Partnerships Act 1907 (UK) (LPA)*	All partnerships are tax transparent, as if there is no separate legal entity.[11] [Income and losses – same as England and Wales]	A Scottish LP must be registered in accordance with the Registrar of Limited Partnership in Scotland.[12] There must be at least one general partner and one limited partner.	Each general partner still has unlimited liability in respect to people who deal with them.[13] [Management role of a limited partner/drawing out contribution same as England and Wales]	A Scottish LP is a separate legal entity (unlike the UK counterpart).[14] The LP, as a separate legal entity, may itself hold property and enter into contracts.[15] There is no automatic dissolution of the partnership when there is a change of partners.[16]
Ireland[17] *Limited Partnerships Act 1907 (UK) (LPA)*	[Same as England and Wales]	[Same as England and Wales]	[Same as England and Wales]	[Same as England and Wales]
United States of America (USA) *Uniform Limited Partnership Act 2001 (ULPA)*	Income, profits and losses are to be shared between the partners in accordance with the agreed proportion stated in the partnership agreement.[18] Distribution is to be shared between the partners on the basis of the value of contributions received from each partner.[19] Income tax is assessed on each partner individual share of profits and losses.[20]	To have a valid LP, a LP certificate must be delivered to the Secretary of State for filing.[21] There must be at least one general partner.[22] A person may act in the capacity of both a general partner and a limited partner, but would be subject to both sets of requirements.[23]	A limited partner has no right or power to act so to bind the LP.[24] Though, a limited partner has a right to information.[25]	It is a separate entity from its partners.[26] A limited partner is not liable for liability incurred from taking an active role in the management of the firm.[27] Most commonly used in the film industry and real estate investment projects.
China *Partnership Enterprise Law, Chapter III (PEL)*	Income is to be distributed in accordance with the agreed proportion stated in the partnership agreement (otherwise, based on each partner's proportional contribution).[28] If the proportion cannot be discerned, then the profits or losses will be distributed equally by the partners. Each partner is assessed individually for its own income tax after distribution.[29]	A LP should be registered at the Enterprise Registration Organ.[30] A LP should have more than 2, but less 50, partners.[31] With at least one 'common partner' (ie general partner). A LP should indicate clearly that it is one.[32] There must be a partnership agreement containing the required information.[33]	A limited partner has no executive rights or powers nor represent the LP externally. It may have some level of participation in management in accordance with the approved actions in the legislation.[34]	A limited partner is only liable to the extent of its capital contribution.[35]

Hong Kong *Limited Partnerships Ordinance (No 37)* (LPO)	Each individual and corporate partner should be taxed on its respective share of the profits and losses and entitled to relief from income tax in accordance with their respective share in the LP.[36] A limited partner's entitlement to losses is limited by its total contribution of capital.[37]	A LP must be registered in accordance with the Ordinance.[38] A LP should have at least one general partner and one limited partner.[39]	A limited partner cannot draw out or receive back any of its contribution during the partnership.[40] A limited partner cannot take part in the management of the partnership business and has no power to bind the firm. (Though a limited partner may inspect the books and examine the state and prospects of business and may advise thereon.) Otherwise the limited partner would lose its limited liability.[41]	A limited partner is only liable to the extent of its capital contribution.[42]
New Zealand *Limited Partnerships Act 2008* (NZ) (**LPA 2008**)	Each partner is taxed individually at that partner's personal tax rate (ie the LP is tax transparent).[43] Each partner's share of the assets is determined by its capital contribution, which represents part of the partnership interest of that partner to the LP.[44] A limited partner's entitlement to losses is limited to '*the partner's basis*' in accordance with HG 11(3) of the *Income Tax Act 2007 (NZ)*.[45] However the denied deduction can be carried forward to the next income year.[46]	A LP must be registered in accordance with section 51 of the Act.[47] This includes an overseas LP that carries on business in New Zealand.[48] A LP should have at least one general partner and one limited partner.[49] There must be a written partnership agreement.[50]	A person cannot be both a general partner and a limited partner of the same LP at the same time.[51] A limited partner must not take part in the management of the LP.[52] A limited partner is not liable for the debts and liabilities of the LP if it does not take part in management.[53] Otherwise it loses its limited liability.[54] A limited partner has no authority to bind the LP or the other partners.[55] A distribution can only be made provided the LP satisfies the solvency test.[56]	A LP has a separate legal personality.[57] A LP has full capacity and powers to carry on business.[58] A limited partner is only liable to the extent of its capital contribution.[59] It is an international preferred structure for investing in venture capital.[60]

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