



Investment & Financial Services Association Ltd

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16 January 2009

The Hon Wayne Swan MP  
Treasurer  
Budget Policy Division  
Department of the Treasury  
Langton Crescent  
PARKES ACT 2600

By email: [prebudgetsubs@treasury.gov.au](mailto:prebudgetsubs@treasury.gov.au)

Dear Treasurer

### ***2009-10 Pre-Budget Submission***

IFSA welcomes the opportunity to contribute to the 2009-10 Budget process.

IFSA is a national not-for-profit organisation which represents the retail and wholesale funds management, superannuation and life insurance industries. IFSA has over 145 members who are responsible for investing over \$1 trillion on behalf of more than ten million Australians. Members' compliance with IFSA Standards and Guidance Notes ensures the promotion of industry best practice.

The 2009-10 Budget will be delivered in the context of challenging economic conditions. The global financial crisis continues to affect financial markets across the globe and is increasingly impacting on the real economy. In this context IFSA has identified a limited range of high priority issues that the Government should address.

### ***Bank guarantee***

The Australian Government's 2008 Deposit and Wholesale Guarantee of Banks and ADIs will have a significant impact on the 2009-10 budget and future estimates. It has helped stabilise financial markets. However, the guarantee has also resulted in market distortions. A comprehensive and transparent evaluation of the costs and benefits of the guarantee needs to be a priority commitment. Furthermore, the government should commit to a forward plan that reduces the scope of the guarantee to minimise market distortions.

IFSA will provide a separate submission to government proposing a way forward on the bank guarantee.

## ***Retirement Incomes***

The global financial crisis has had a massive impact on financial markets, and therefore on the savings of Australians. The most notable impact has been the massive shift in investment returns, swinging from 5 years of almost unprecedented strong investment returns to a once in a generation market downturn.

It would be easy to ignore retirement income policies given these developments. This would be the wrong approach. IFSA strongly supported the Rudd Government's decision to prioritise the examination of Australia's retirement income system through the Australia's Future Tax System (AFTS) review.

The age pension plays an important role in delivering a basic retirement income to Australians, but it is the superannuation system which holds the key to improving the quality of life of Australians retiring in the future and improving the long-term fiscal sustainability of the Australian Government.

IFSA will be making detailed submission on retirement income issues to the AFTS Review Panel. The 2009-10 Budget should include the Government's response to the AFTS Review recommendations on superannuation adequacy and related issues, such as removing barriers to innovative retirement income products. Policy changes for retirement income adequacy will take time to have some effect. Steps therefore need to be taken as soon as possible to address challenges that Australia will face in 20 to 30 years time.

## ***Product Rationalisation***

The global financial crisis heightens the need to introduce initiatives such as a product rationalisation mechanism to maximise the efficiency of Australia's financial services industry.

The law provides a framework within which financial products can be developed and offered to customers. Various amendments to the law, taxation and technological advances over the last 20 years have meant many products lack the features and functionality of today's financial product offerings. Given that financial products are designed and created at a point in time in a particular legislative and technological environment, products will, over time, become outdated and difficult to maintain.

The absence of a simplified process enabling financial products to be rationalised increases costs to the financial services industry and its customers. In 2005, IFSA estimated that the annual economic benefits resulting from the removal of existing legal barriers to product rationalisation would be between \$120 million (conservative estimate) to \$350 million (optimistic estimate). This represents the equivalent of approximately \$70 per year per customer in a legacy product.

IFSA made a comprehensive submission to the then Government in 2005 calling for legislation to facilitate product rationalisation. IFSA recommends that the 2009-10 Budget announce the introduction of a product rationalisation regime covering managed investments, life insurance and superannuation along the lines IFSA has outlined. Any reduction in the scope of proposed product rationalisation measures should be rejected as it has the potential to significantly reduce the benefits to consumers and industry in terms of costs and efficiency.

## ***International Financial Centre***

The global financial crisis should also be seen as an opportunity to further the Rudd Government's agenda to make Australia an international financial centre. Australia's financial services industry is better placed than many of our global competitors to emerge from the crisis in a strong position. This strengthens the case for sensible government initiatives to facilitate higher financial services exports.

The introduction of a world class managed investment tax regime is essential if Australia is to be able to compete as an international financial centre.

The Board of Tax is currently conducting a Review of the Tax Arrangements Applying to Managed Investment Trusts. As the Board of Tax has been requested to provide its report to Government by June 2009 the Government's response would not be included in the 2009-10 Budget.

Nevertheless, this review, and in particular a resolution on the capital versus revenue account treatment of gains and losses made on disposal of investment assets by MITs, is a high priority for IFSA.

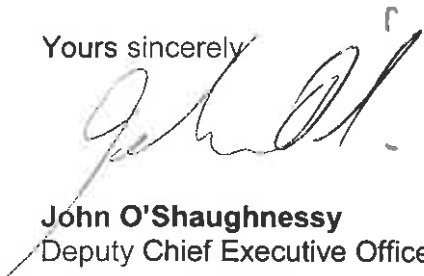
In addition to the introduction of a managed investment tax regime, IFSA has been actively involved in a number of Australian Government initiatives aimed at further developing Australia into an international financial centre.

Most recently, IFSA lodged a submission in December (together with the members of the Finance Industry Council of Australia) to the Australian Financial Centre Forum outlining a series of recommendations which should be implemented in the 2009-10 Budget.

The Attachment highlights three initiatives as key priorities: introduce an Investment Manager Exemption; exempt managed funds from the Foreign Investment Fund rules; and, provide additional targeted resources for Austrade and the Australian Bureau of Statistics. The tax measures are not expected to impose a significant cost to revenue and in some cases, IFSA believes these reforms could increase revenue from the resulting expansion of economic activity.

Should you have any questions regarding the submission, please contact me on 02 9299 3022.

Yours sincerely



**John O'Shaughnessy**  
Deputy Chief Executive Officer

## **AUSTRALIA AS AN INTERNATIONAL FINANCIAL CENTRE**

### **Introduce an Investment Manager Exemption**

The introduction of an 'Investment Manager Exemption' will ensure foreign source income flowing through to non-residents is not taken to be Australian source income under Australian tax law and therefore not subject to Australian tax.

Australia is out of step with most leading international financial centres in terms of the treatment of foreign investors in Australian managed funds. Consequently, significant flows of capital, particularly from Asia, will continue to remain outside Australia, with a detrimental impact on employment and economic growth.

This is especially cumbersome and results in a lost opportunity for Australians and the Australian economy. Australian fund managers are often considered to be some of the best in the world yet in order to compete they often end up having to establish operations overseas to apply their expertise. Clearly this issue has become even more important given the current economic crisis.

As such, it is important that Australia provide exemptions that are at least equivalent to those offered overseas.

In this regard, the United Kingdom has an 'investment management exemption' which allows a manager acting for a non-resident to be exempt from assessment on behalf of its non-resident client, including offshore funds. The exemption was introduced to encourage non-residents to invest through British institutions.

In the US, the exemption for foreign investors trading in US stocks even where a local agent / manager is present in the US has been in place for many years. Hong Kong has also implemented such an exemption clarifying that offshore funds with Hong Kong fund managers and investment advisors may now confidently state that they are not subject to tax in Hong Kong on profits derived in Hong Kong.

A similar exemption could be used in Australia, to address situations in which Australian and foreign source income flowing through to non-residents is taken to be Australian source income under Australian tax law because the management and control function is performed by an Australian fund manager. So doing would provide a significant boost to the export activities of the funds management industry.

### **Exempt Managed Investment Funds from the Foreign Investment Fund rules**

IFSA recommends that the Government introduce an appropriate FIF exemption for managed funds where:

- (a) Registered Managed Investment Schemes or a unit trust, all of the units of which are held by Managed Investment Schemes and/or complying superannuation funds;
- (b) Such funds would be required to satisfy a widely held test (as per s12-395 of the Taxation Administration Act 1953);
- (c) For investments in entities resident in jurisdictions with which Australia has entered into a Double Tax Agreement; or
- (d) The offshore vehicle distributes a large proportion of its income.

Such an exemption would considerably reduce the compliance burden on the industry without giving rise to significant risks to the Revenue.

These are longstanding issues which have been identified by industry over many years and their implementation would provide a significant impetus to the development of Australia into an international financial centre.

### **Additional targeted resources for Austrade**

In order to more effectively facilitate cross-border financial services activity, Austrade will require designated in-country financial services resources in key markets.

The industry's previous experience with delegations and country missions has been very positive and Austrade's assistance has been essential in ensuring the success of these missions.

Going forward however, in order to build on these missions and to enable more and deeper market intelligence to be actively shared between industry and Austrade, a greater level of financial services experience and expertise will be required within Austrade. Such expertise will also be of great use in providing practical input into relevant FTA and multilateral trade negotiations.

Additionally, Austrade is expected to be a driving stakeholder in the development of a consistent brand and promotional strategy for the Australian financial services industry that is aimed at:

1. Increasing the level of regional awareness of the Australian financial services industry, its strengths and capabilities.
2. Attracting increased capital flows into Australia.
3. Lowering off-shore barriers and obstacles facing the Australian financial services industry.
4. Attracting new entrants to the Australian market.

In addition to the support of industry, this exercise will require specific funding to ensure it delivers on the above objectives. If it were to take on the role, Austrade would require funding to deliver:

- a design agency brief to enable the creation of an Australian financial services brand;
- a promotion strategy covering Government, industry & relevant stakeholders; and
- Guidelines to support the brand.

Industry strongly supports Austrade's role in the development of a consistent brand and promotional strategy for the Australian financial services industry.

### **Collection of Data on Australia as an International Financial Services Centre**

IFSA supports additional specific purpose funding for the Australian Bureau of Statistics (ABS) to significantly improve the quality of data collected and published on funds management cross-border flows. This funding would benefit public policy decision making in areas such as Free Trade Agreement and Double-Tax Agreement negotiations, as well as regulatory mutual recognition discussions.

At present, the only official data available on managed funds is that provided in the ABS Catalogue 5655.0 Managed Funds, Australia.

In respect of cross-border capital flows, this catalogue uses aggregated categories titled 'funds from overseas' and 'assets overseas' for total assets derived from overseas sources and total assets held overseas respectively.

This aggregation leads to the following gaps:

- The data does not capture *flows*, rather just the total *stock* at a given point in time, making it more difficult to assess trends in cross-border fund movements.
- The Catalogue does not currently provide details on the asset classes into which these funds are invested (either domestically or overseas). For example, there is no breakdown of either flows or the stock of funds according to: equities, real-estate investment trusts (or LPTs), fixed interest, private equity, alternative assets, etc.
- In relation to the aggregate 'funds from overseas' and 'assets overseas', neither the country source nor country destination is currently disclosed. This information would be particularly useful in assessing the success of government initiatives to facilitate Australia's export of financial services across different markets. More specifically, it would allow vital information on funds flows to be utilised for the benefit of negotiations around mutual recognition agreements between country regulators, free trade agreements and even double tax agreements.
- Further transparency with respect to the form of the cross-border flows would also be desirable beyond merely "direct" and "indirect" classifications. This would provide a more in-depth understanding of the investment vehicles being used by foreign investors investing in the Australian market and vice-versa.

In addition to improving the quantity and quality of funds management data, the ABS could partner with industry in producing a related data series designed to measure the value of funds management exports.

This would data series would ideally take account of the "cluster of services" that necessarily attaches to the provision of any funds management service.

Specifically, this "cluster of services" includes: Asset management; Investment consulting; Platform delivery systems; wrap accounts and master trusts; Custodial and registry services; Financial service IT and software; development providers; Actuarial services; Legal and accounting services; Compliance and risk monitoring; Investment performance research and reporting; Education and training services; Portfolio administration services; as well as Advice/distribution.

While the ABS does currently measure 'exports of financial services' in catalogue 5368.0 International Trade in Services and associated sub-catalogues, it does not take account of the value of these attaching financial services.

IFSA notes that private sector research houses have questioned the ABS' calculations in terms of total funds under management as well as the proportion of funds sourced from offshore. IFSA would be pleased to arrange a series of industry roundtables with such research houses and the ABS, Treasury and other relevant stakeholders to contribute towards the development of more detailed and robust data on our industry.