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25 June 2015

2015/21

Tax insights

Investment Manager Regime (IMR) law enacted

Snapshot

On 25 June 2015, the legislation containing the third and final element of the Investment Manager Regime (IMR 3) received Royal Assent, and is now enacted law. This is the culmination of a lengthy process commencing in December 2010. This legislation follows on from a Bill that was introduced into Parliament in May 2015: a copy of the May 2015 tax insights can be viewed here. A number of last-minute changes were made to improve the operation of the IMR.

The IMR should be welcomed by non-Australian residents such as hedge funds investing in Australia, and funds which engage independent Australian fund managers. Funds should undertake an IMR review to determine whether they qualify for the IMR concession for any year (including prior years) in which income or gains from investments might otherwise be subject to Australian tax.

IMR 3 as enacted

The stated objective of the IMR is to encourage particular kinds of investment made into or through Australia by certain non-Australian residents that have wide membership, or that use Australian fund managers. This is achieved by providing non-Australian residents with an Australian income tax exemption for income or gains in respect of the disposal of their investments that otherwise might be sourced in Australia and subject to Australian tax.

A comprehensive analysis of the provisions of the IMR is contained in the May 2015 tax insights. Between the introduction of the Bill into Parliament in May 2015 and final passage by Parliament, there were a number of changes made to improve the operation of the IMR, and these are summarised below:

Sub-underwriting arrangements

In respect of the indirect concession involving an independent Australian fund manager, a sub-underwriting fee may qualify for the IMR concession where the underwritten interests are themselves IMR financial arrangements. This does not apply in the case of the direct concession.

Scope of eligible income

The revised Explanatory Memorandum states that

- Amounts paid to an IMR entity as compensation for a loss suffered directly as a result of an act done, or an omission, by the independent Australian fund manager is income that relates to an IMR financial arrangement; and
- A foreign exchange gain from normal expense accruals of the fund (such as related management fees) that would otherwise be assessable should qualify for the IMR concession, provided they do not relate to anything other than one or more IMR financial arrangements of the IMR entity.

Participation interests of fund managers

In applying the widely held tests, participation interests that relate to entitlements to remuneration can be disregarded (subject to certain conditions) whether the fund manager is an independent Australian fund manager, or an independent foreign fund manager.

Limited partnership definition

Aspects of the finalised IMR rules can be applied on an optional basis for periods to 30 June 2011, covered by enacted IMR 1, to ensure that the IMR 1 rules operate as intended. It is proposed that the amendments dealing with the residency of a limited partnership will also be applicable for periods to 30 June 2011.

Next steps

Funds should undertake an IMR review to determine whether they qualify for the IMR concession for any year (including prior years) in which income or gains from investments might otherwise be subject to Australian tax. This will require detailed fact-finding, accompanied by a thorough technical analysis for each relevant fund to test the fund's status in respect of all relevant years as an eligible fund, and to test that all income otherwise subject to Australian tax is exempt under the IMR concession.

As a starting point, some of the questions that fund managers should focus on in order to determine whether a fund is eligible for the IMR concession are as follows:

For what years does a fund have a potential exposure to Australian tax?
For periods prior to 30 June 2011 (note that the indirect concession is not available for this period):

- Does the fund qualify as widely held under IMR 1 as enacted?
- Does the fund qualify as widely held for IMR 1, as amended by the IMR 3 widely held tests?
- Is the relevant income "IMR income"?

For periods after 30 June 2011:

- Is the relevant concession the direct or indirect concession, or both?
- Does the fund qualify as widely held?
- Is any Australian fund manager an "independent Australian fund manager"?
- Does all relevant income qualify for the concessions?

In addition, fund managers should consider:

- Should funds establish or make greater use of Australian fund managers?
- Do any other operational aspects of the fund need to be reviewed in light of the finalisation of the IMR?

Contacts

For more information, please contact

Vik Khanna
Partner
+61 (3) 9671 6666
vkhanna@deloitte.com.au

David Watkins
Partner
+61 (2) 9322 7251
dwatkins@deloitte.com.au

Mark Hadassin
Partner
+61 (2) 9322 5807
mhadassin@deloitte.com.au

Julien Cheng
Partner
+61 (2) 9322 7000
jcheng@deloitte.com.au

For further information, visit our website at www.deloitte.com