2 November 2000

Assistant Commissioner
Law Design & Development (Entities)
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Dear Assistant Commissioner

## Entity Taxation Exposure Draft
## Submission: Argo Investments Limited

We refer to the Exposure Draft *New Business Tax System (Entity Taxation) Bill 2000* ("the Exposure Draft") released by the Government on 11 October 2000. Argo Investments Limited ("Argo") wishes to bring to your attention some concerns which it has in relation to entity taxation and the proposed restructure relief.

## Overview

Under the Exposure Draft, entities that qualify as Fixed Trusts will maintain 'flow through' taxation treatment. Accordingly, capital gains derived by Fixed Trusts will continue to flow through to individual investors who can obtain the benefit of the 50% CGT exemption.

Listed Investment Companies ("LICs"), such as Argo, are put at a significant disadvantage compared to Fixed Trusts as shareholders are unable to benefit from the CGT concessions.

The Exposure Draft provides transitional restructure relief for companies such as Argo to convert to a Fixed Trust structure. This submissions outlines the reasons why restructure is not a viable option for Argo. In addition, we suggest a solution to the problem which will achieve an equal taxation treatment for all investors.

## Conversion to a Fixed Trust is *not* the solution

The conversion from a company structure to a Fixed Trust is not economically feasible for companies such as Argo for the following reasons:

*1. Commercial advantages of LICs compared to Fixed Trusts will be compromised*

The advantages of investing in a LIC as opposed to a Fixed Trust include:

- significantly lower management expense ratios (MERs). Argo has a MER of less than 10% of the MER of an equivalent Fixed Trust;
- no intermediaries charging additional fees to investors;

- a structure which enables adoption of a long term investment approach, rather than the short term approach required by a Fixed Trust that must be prepared to redeem its holders' units at short notice;
- simpler administrative structure provided by stock exchange listing;
- the existence of a liquid market for investments in LICs due to stock exchange listing, providing easy and economic entry to, and exit from, the investment;
- no entry or exit charges are made by LICs;
- greater transparency of operations due to regulations (eg ASX Listing Rules) covering publicly listed vehicles.

If Argo is required to convert to a Fixed Trust structure to remain attractive to retail investors, the competitive advantages outlined above will be lost.

*2. Additional costs of converting to a Fixed Trust*

In addition, Argo will incur substantial costs if required to convert to a Fixed Trust structure. Such costs would include:

- compliance with the Managed Investments Act, both in establishing the Fixed Trust structure and in the ongoing operations of the Fixed Trust. This merely duplicates the protection already afforded to shareholders via the provisions of the Corporations Law and the ASX Listing rules as applicable to listed entities;
- preparation and registration of an annual Prospectus/Public Offer Documents and Trust Deed;
- stamp duty incurred on transfer of assets from the Company structure to the Fixed Trust structure.

*3. Proposed restructure relief provisions are uneconomical*

The proposed rollover provisions contained in the Exposure Draft will impose unnecessary costs on LICs such as Argo. In particular:

- the requirement to liquidate Argo within 6 months of the restructure will be expensive;
- Argo will require a "Single Responsible Entity" to be a "Managed Investment Scheme" under the MIA. This will require a new entity to be established resulting in further costs.

## Solution

A simple solution to the above would be to allow LICs such as Argo to flow through capital gains to its shareholders. This would allow individual investors in LICs to obtain the CGT exemption in the same way as an investor who invests either directly or through a Fixed Trust structure per the exposure draft.

This can be achieved as follows:

- maintenance of a separate "Capital Profits Account" by LICs to record profits taxed in the company as capital gains. This account would be similar in concept to the existing "Foreign Dividend Account" or the proposed "Foreign Income Account".

- dividends paid from the Account will be separately identified on the shareholder's dividend statement and will be taxable to shareholders as capital gains and will carry full franking credits for tax paid at the company level.

The Australian Taxation Office (ATO) will obtain a timing advantage where the individual invests through a LIC, as the company pays tax on the gain up-front at the rate of 30% (as opposed to an individual at an effective maximum rate of 24.25%).

We are able to provide you with working examples of how this proposal would work along with comparisons to fixed trusts and direct investments.

In order to meet the objectives of the Ralph Committee to tax all entities equally, Argo submits that the benefits available to Fixed Trusts under the Exposure Draft should be extended to LICs.

Argo welcomes the opportunity to participate in any discussions in respect of the concerns that we have raised and the development of the Government's Exposure Draft.

If you or any member of your office would like to discuss any aspect of this submission, please contact me on (08) 8212 2055.

Yours faithfully
ARGO INVESTMENTS LIMITED

R.J. Patterson
Managing Director