

18 December, 2000

Assistant Commissioner  
Law Design and Development (Entities)  
Australian Taxation Office  
PO Box 990  
Civic Square  
CANBERRA ACT 2608

Dear Sir

### **Entity Taxation - Exposure Draft Legislation**

I refer you to the Entity Taxation Exposure Draft Legislation released on 10 October 2000. We are writing to draw to your attention the consequences of two of the measures contained in the draft. They relate to the definition of a fixed trust and the availability of rollover relief.

We submit that the draft legislation should be amended to:

- ensure that trusts such as the Grand Hotel Trust, will qualify as fixed trusts.

### **Grand Hotel Entities**

Grand Hotel Trust (the **Trust**) and Grand Hotel Company Limited (the **Company**) own and operate, respectively, a number hotels in Australia including several Hyatt hotels. Shares in the company are stapled to units in the Trust. There are 177,907,288 stapled securities which are listed on the Australian Stock Exchange and are held by a range of institutions, companies and individuals. The Trust is a passive investor and its only activities are to:

- lease the hotel properties to the Company;
- make loans to the Company;
- lease hotels to independent operator companys.

### **Impact of proposals contained in Draft Exposure Legislation**

- **Definition of a fixed trust**

The Exposure Draft Legislation (the **draft legislation**) proposes to tax non-fixed trusts in a similar manner to companies. The draft legislation adopts the definition of a fixed trust contained in Schedule 2F of the *Income Tax Assessment Act 1936*. This definition requires unitholders to have a vested and indefeasible interest in a trust before the trust qualifies as a fixed trust.

Section 272-5(2) of Schedule 2F of the *Income Tax Assessment Act 1936* broadly states that where a trust deed gives the trustee the power to issue or redeem units at market value, the unitholders will not be considered not to have a vested and indefeasible interest, simply because the trust deed gives the trustee this power.

Therefore, where a trust deed allows units to be issued at less than market value in any circumstances, the unitholder may not have a vested and indefeasible interest and hence the trust will not be a fixed trust. The argument being that if a trustee has a power to issue new units at less than market value, the existing unitholders' interests are defeasible, as the trustee may dilute the value and proportion of the existing unitholders' interest by issuing more units at less than market value.

- **The Trust's Deed**

The Trust's constituent deed, in common with the trust deeds of most other public unit trusts, provides that the unitholders are presently entitled to the income and capital of the Trust. In addition, it specifies the circumstances in which units may be issued, redeemed or capital distributed to the unitholders.

- **Placements**

The Trust deed contains a clause that allows for the issue of units at a price that is not less than 50% of the market value in certain circumstances. This clause allows for the issue of up to 10% of the number of the existing units in a placement at a price determined by the Trustee, subject to unitholder approval where the discount exceeds 10%. A private placement on these terms is permitted by the *Corporations Law*.

Where the stapled securities are trading below their Net Tangible Asset backing, there may be circumstances in which a placement may be undertaken at higher than market value ie higher than the then current trading price. The Entity Taxation legislation also needs to make it clear that unit issues at greater than market value do not affect a trust's fixed status.

- **Distribution Reinvestment Scheme**

The Trust deed also allows for a possible distribution reinvestment scheme, under which unitholders may elect to reinvest their distributions in units, with a purchase price that is not less than 50% of the market value of a unit.

- **Partly paid units**

The Trust deed also allows for the issue of partly paid units. These units are entitled to income and capital on a *pari passu* basis. The draft legislation should make it clear that holders of partly paid units participating *pari passu*, rather than on a full unit entitlement, does not affect the fixed nature of the trust.

## **Result**

Arguably, based on the current definition of a fixed trust, the ability of the Trustee to undertake these types of commercial capital management measures will cause the Grand Hotel Trust be a non-fixed trust and hence to be taxed as a company. This would be a manifestly absurd result and clearly not one that the Government intends. Not only the Grand Hotel Trust but a majority of listed unit trusts would be classified as non-fixed trusts if the current intended approach is not clarified. Most of them would have qualified as collective investment vehicles ("CIV's") under the Review of Business Taxation proposals, and would have been taxed as trusts rather than as companies under that regime.

All of these trusts are public investment vehicles with large numbers of disparate investors. To suggest that their interests are not fixed is inconsistent. The Australian Securities and Investment Commission could not have cleared the prospectuses for these trusts on that basis.

If you require further information, please contact Wayne Brown of my office, on 9667 8893.

Yours faithfully,

Garry Cameron  
Managing Director