

2 November 2000

Assistant Commissioner
Law Design & Development (Entities)
PO Box 900
Civic Square
CANBERRA
ACT 2608

By facsimile: (02) 6216-1852

Dear Sir,

Entity Taxation

We are writing to comment on the Entity Taxation exposure draft, which was released on 11 October 2000.

Templeton Investment Management (Australia) Limited has been an active participant in the Australian financial services industry since 1990. In particular, we manage an Australian registered unit trust, Templeton Global Trust Fund, and an associated investment company, Templeton Global Growth Fund, Ltd., has been listed on the Australian Stock Exchange since 1987. In addition, we have been actively seeking to distribute, in Australia, US mutual funds managed by our parent organization, the Franklin Templeton Group.

The proposed legislation contained in the Entity Taxation exposure draft fails to satisfy the investment neutrality principle¹ contained in the recommendations of the Ralph Inquiry. Further, the legislation fails to satisfy the competition objectives of the Wallis Inquiry² and effectively defeats the Foreign Investment Fund exemption for US mutual funds³.

The draft legislation will generate different after tax returns for Australian investors depending on the vehicle they choose to undertake investment in either Australian or foreign equity securities. The attached schedule summarizes the after tax returns for Australian individuals or superannuation funds investing in a portfolio of global equity securities either directly, or through a fixed trust, a US mutual fund organized as a corporation, or an ASX listed investment company. For example, direct

¹ Policy Design Principle P1 – Page 111, “A Tax System Redesigned”.

² Treasurer’s announcement, December 1997 – “Australia – A Regional Financial Centre”.

³ Taxation Laws Amendment Act (No. 2) 1999.

investment in a portfolio of global equity securities will generate superior after tax returns to investing in the same portfolio via a fixed trust. Similarly, investment through a fixed trust will generate superior after tax returns to investing through an ASX listed investment company or a US mutual fund, organized as a corporation. Investment in Australian equity securities, either directly, or through any of the above investment vehicles will produce consistent after tax returns.

If the draft proposals are implemented, the average Australian investor will be encouraged to invest directly in a potentially riskier, self-managed portfolio of securities rather than via a professionally managed, diversified investment fund. Further, ASX listed investment companies and US mutual funds, organized as a corporation, will be less attractive to Australian investors as these investment vehicles will not receive the same concessional capital gains treatment as fixed trusts. We believe that these outcomes are not desirable from either a national savings or competition perspective.

If the government's desire is to promote saving by individuals and to encourage vigorous competition in the Australian managed funds industry, then the Entity Taxation legislation should satisfy both the Ralph investment neutrality principle and the Wallis competition objectives. In other words, Australian individual and superannuation fund investors should receive the same capital gains tax treatment whether they invest in fixed trusts, ASX listed investment companies, US mutual funds, or directly in investment securities. Accordingly, we believe that the Entity Taxation exposure draft should be amended so that all the above investment vehicles are treated on a tax-neutral basis with direct investment.

We would welcome the opportunity to discuss our concerns with the Commonwealth Treasury. Please telephone me on (03) 9866-3562 if you should require any additional information.

Yours sincerely,

Geoffrey N Webb
Executive Director