



Australian Foundation
INVESTMENT COMPANY

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Board of Taxation

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19 November 2008

The Board of Taxation
c/o The Treasury,
Langton Crescent,
PARKES
ACT 2600

Dear Sir or Madam,

**SUBMISSION WITH REGARDS TO THE REVIEW OF THE TAX
ARRANGEMENTS APPLYING TO MANAGED INVESTMENT TRUSTS**

The Board of Taxation has called for written submissions from the Australian community with regards to the Discussion Paper issued in October 2008 relating to the tax arrangements applying to Managed Investment Trusts.

I am writing as Managing Director of Australia's largest Listed Investment Company, Australian Foundation Investment Company (AFIC) representing over 88,000 shareholders, primarily domestic and retail. We commenced operations in 1928. Shareholders invest with us as an alternative to Managed Investment Trusts. Our investment approach gives them a comparatively inexpensive way of accessing capital growth over the medium to long-term as well as to access fully-franked dividends that the Company seeks to increase faster than the rate of inflation.

From 1999 the Government changed the law on Capital Gains Tax to provide for individuals to be exempt from Capital Gains Tax on half the capital gain made on the sale of securities held more than one year and for superannuation funds to be exempt from one third of the gain (referred to as the 'concessional CGT treatment'). As a result of the flow through nature of the Investment Trust structure this meant that unit holders in Managed Investment Trusts also had access to that concessional CGT treatment provided that the nature of the trust's transactions were capital.

This placed Listed Investment Companies (LICs) such as Australian Foundation Investment Company Limited at a disadvantage to Managed Investment Trusts. After agitation by the LICs and their shareholders, legislation was introduced to enable shareholders in LICs to claim a tax deduction in respect of dividends paid out of realised capital gains to ensure that shareholders were treated equivalently compared with investors in managed investment trusts who were able to access the concessional CGT treatment when shares that had been held by the trust for more than one year on capital account were sold.

AFIC's business affairs are such that they are in accordance with the guidelines laid down in Taxation Ruling 2005/23, on Income Tax: Listed Investment Companies, and it has both a trading account where securities are held for profit making on sale and any gains made are on revenue account and a long-term investment portfolio where investments are held on capital account. AFIC therefore understands and is compliant with the current arrangements with regard to the separation of gains made on revenue and gains made on capital. Accordingly, we are able to make available to our shareholders the special LIC capital gains tax deduction in respect of realised capital gains we have made on investments held for more than one year.

Our understanding is that the Government, as part of the taxation review, is now considering legislation to clarify for Managed Investment Trusts whether the transactions they undertake are on capital account or on revenue account.

We believe strongly that the underlying policy in this area should be based around a level playing field for all pooled managed investment vehicles, whether trusts or companies, to avoid distorting the investment markets, creating uncertainty and making Australian pooled managed investment vehicles less competitive than foreign vehicles:

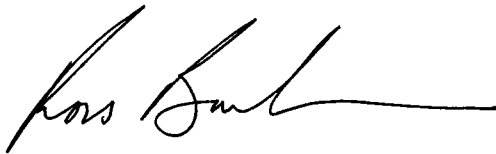
- (a) Whatever treatment applies for Managed Investment Trusts should also apply for LICs. Our preferred solution to the issue would be for legislation that provided for both Managed Investment Trusts and LICs to have transactions treated in the same way as legislation currently provides for superannuation funds. That is to say, that all transactions that are undertaken are on capital account, but with concessional CGT treatment for shares held more than one year.
- (b) Our primary concern is to ensure that there is still equivalent treatment of transactions as between Managed Investment Trusts and LICs so that investors in one structure are not unfairly treated in comparison with the other.

We note that the current discussion paper does not envisage any change to the treatment of capital gains for individuals, so we favour a structure that provides for pooled managed investment vehicles, whether trusts or companies, to provide a similar outcome. There are advantages, particularly for small shareholders, in accessing equity markets through pooled investment vehicles rather than directly individually, namely the benefits of diversification, economies of scale and management costs shared across a wide pool of investors.

Needless to say, we would be very concerned regarding any change in legislation that all gains made from investments should be on revenue account. Such a move would severely disadvantage smaller retail investors who choose to invest through managed investment vehicles such as LICs.

I would be happy to expand on any of the above points at your request.

Yours sincerely

A handwritten signature in black ink, appearing to read "Ross Barker", with a long horizontal flourish extending to the right.

Ross Barker
Managing Director