

29 June 2002

Mr George Montanez
Executive Officer, International Tax Division
Australian Taxation Office
2 Constitution Avenue
CANBERRA ACT 2600

Lawyers

Levels 22-35
No.1 O'Connell Street
Sydney NSW 2000
Australia

PO Box H3
Australia Square
Sydney NSW 1215
DX 370 Sydney

Tel + 61 2 9353 4000
Fax + 61 2 8220 6700
www.claytonutz.com

**Sydney · Melbourne
Brisbane · Perth
Canberra · Darwin**

Our reference
227/21719435

Partner
Mark Friezer

Dear Mr Montanez,

**Australian Securitisation Forum
Thin Capitalisation**

We refer to the proposals recently circulated by Kim Salisbury in relation to securitisation and the zero capital concession.

Thank you very much for the work that you and your colleagues have put into dealing with the ASF's concerns on Thin Capitalisation.

I have set out below, on behalf of the Australian Securitisation Forum ("**ASF**") our comments in relation to the proposals:

1. **Technical Comments**

(a) **Proposal to delete/replace the current definitions of "Securitized Assets" and "Securitisation Vehicle".**

The proposals recommend that the definitions in the current legislation of "Securitized Assets" and "Securitisation Vehicle" be deleted. Notwithstanding we do not believe that the current definitions are satisfactory, it is the case that various parties have structured their affairs in order to comply with the current concepts. Rather than deleting the existing definitions we suggest that the existing rules continue to have effect. In other words any new rules should have effect retrospective to the date that the thin capitalisation regime applies and would operate alongside the existing rules. The existing rules could be phased out, say, 12 months after the introduction of the new rules.

(b) **The tests for a "Securitisation Vehicle" should not be cumulative.**

As the proposed rules are currently drafted, for a vehicle to qualify as a "Securitisation Vehicle" it must satisfy both the APRA prudential standards and the Australian Accounting Standards. This requirement gives rise to a significant additional compliance burden in that securitisation vehicles will need to monitor and take advice in relation to two sets of rules for tax purposes which are otherwise not relevant to them.

The ASF believes that these tests are more appropriately expressed in the alternative. For example, the ASF believes that where it can be demonstrated that the application of accounting standards would not require the recognition of debt on

the sponsor's balance sheet, this should be sufficient so that the debt is not recognised under the thin capitalisation rules.

In order that the position of the securitisation vehicle can be determined with greater certainty we suggest a provision which provides that certification of the accounting position by a registered auditor is definitive (that is 'post Enron' accounting sign offs for matters that will expose accountants to risk of suit will be harder to obtain, and we think it preferable if the test is, in effect, that the accountants have signed off, rather than they have signed off and are not wrong).

(c) **De minimis concession.**

The proposed rules as presently drafted do not allow any level of credit support. We reiterate the view we have previously expressed that provision of a level of credit support up to a certain percentage of the value of securitised assets should be allowable. The ASF believes that an appropriate percentage for this purpose would be 8%.

(d) **Election for originator/seller or vehicle sponsor to recognise debt.**

We propose that in addition to (a), (b) & (c) a joint election be available whereby a "Securitisation Vehicle" (that is either a trust or company) and the originator/seller of assets or sponsor of the vehicle could elect, for thin capitalisation purposes only, for the special purpose vehicle to be consolidated with the originator/seller or the sponsor. Where this election is made the thin capitalisation rules would not apply to the "Securitisation Vehicle".

This will operate as a "bright line" fall back which provides a means for ensuring, with complete certainty, that the thin capitalisation rules will not apply to the vehicle but that the relevant debt is included on the balance sheet of the originator/seller (or its group) or the sponsor for thin capitalisation purposes. This treatment should address any ATO concerns that securitisation opens the possibility of in effect raising finance whilst not increasing debt levels for thin capitalisation purposes.

This measure could be introduced upon finalisation of the consolidation reforms anticipated in the new financial year.

(e) **Joint & several liability concerns for securitisation vehicles**

As a separate matter, we note a concern which has arisen for securitisation vehicles out of the consolidation rules. This concern is relevant where the securitisation vehicle is a 100% owned entity. Under the provision is made for a tax sharing agreement to be entered into whereby a consolidated group may agree to the sharing of tax liabilities. However, such tax sharing arrangements are heavily qualified. The contributions required of each group member under the tax sharing agreement must represent a reasonable allocation of the tax liability of the group. We propose that securitisation vehicles be accepted by the ATO as entities that are never subject to joint and several tax liability of the consolidated group that they are a member of. This could be achieved by either excluding securitisation vehicles as consolidatable entities for consolidation purposes generally or, if that is not acceptable to the ATO, at least having a confirmation from the Commissioner that no allocation of a group's tax liability to a securitisation vehicle member other than the tax liability that would flow if the vehicle was actually a non consolidated entity, is a reasonable

allocation for the purposes of the group's tax sharing agreement.

Further, when the election proposed at (d) above is made the securitisation vehicle's debt goes onto the seller/sponsor or originators' (or the group of which they are a part) balance sheet for thin capitalisation purposes and is excluded from:

- (i) the securitisation vehicle's balance sheet (when it is not a member of a consolidated group) or;
- (ii) its group's balance sheet (if the seller/sponsor or originator that elects to take the debt is not also a member of the group that the securitisation vehicle is a member).

(f) **Pooled Assets**

In the proposal the definition of a securitisation vehicle refers to one with the "purpose of pooling assets funded by...". We assume that the word 'pooling' is flexible to cover single asset securitisation vehicles (that will not or may not, acquire more than one asset, for example the rental flows from a single building). If so the phrase "pooling assets" in the proposed definition could be replaced with "acquiring one or more assets".

2. **The way forward**

We assume that draft legislation will not issue prior to 30 June and that a press release about the form of proposed legislative amendments to the thin capitalisation rules for securitisation vehicles is also unlikely by that time.

However, as you know, the ASF considers it very important (to the integrity of the Australian Financial Markets) that some comfort be given to the securitisation industry prior to 30 June 2002 in respect of transactions entered into in the year ended 30 June. We hope this takes the form of a letter to the ASF [ABA & IBSA] to the following effect:

"The ATO is reviewing the position of Securitisation Vehicles and is consulting with industry bodies. At this stage it is envisaged that the proposals for supplementing the current rules will be announced in the near future and that such additional measures will have retrospective effect to the commencement of the thin capitalisation regime.

The ATO is also considering the impact of the proposed consolidation rules upon securitisation vehicles and what is an appropriate allocation of a group's tax liability to them under a Tax Sharing Agreement."

Should you wish to discuss these issues further please do not hesitate to contact me, or Charles Armitage of Allens Arthur Robinson or David Temby of Mallesons Stephen Jaques.

Once again thank you for your continuing efforts to resolve the ASF's concerns by 30 June.

Mr George Montanez
Executive Officer, International Tax Division
Australian Taxation Office

8 October 2002

Yours faithfully
CLAYTON UTZ

Mark Friezer
Partner
9353 4227
mfriezer@claytonutz.com