s.22(1)(a)(ii)

From: Maloney, Matthew
Sent: Tuesday, 13 March 2018 2:09 PM
To: s.22(1)(a)(ii)
Cc: Fraser, John (Secretary); Mrakovcic, Maryanne; Brennan, Michael; Gaetjens, Philip; RG TAD SES; McCullough, Paul; Jeremenko, Robert; s.22(1)(a)(ii) Dowdell, Michelle; s.22(1)(a)(ii) s.22(1)(a)(ii)
Subject: RE: Refundability of franking credits [SEC=PROTECTED]

Hi s.22(1)(a)(ii)

We have checked the statements you sent through (some comments below). Let me know if you need anything further.

Labor's policy will reduce the income of more than one million individuals – more than half of whom are over 65 years of age;

- Correct – although it would be more accurate to say it will reduce the tax refund of individuals (i.e. cash in pocket) as taxable income will be unchanged.

Labor's policy will also hit a third of all SMSFs, impacting 370,000 member accounts, and affect retirement savings held in approximately 3.5 million super fund accounts;

- Correct – around 40 per cent of SMSFs receive a refund (200,000 out of 480,000). The account figures (3.5m) are correct but it might be worth pointing out that these are APRA superannuation fund accounts.

Despite Labor's suggestion that recipients of imputation credit refunds are "typically wealthier retirees", almost 9 out of every 10 individuals (85%) who receive franking credit refunds have income below $87,000;

- 85 per cent of the **value** of refunds go to individuals with a taxable income below $87,000. By number more than 9 in 10 individuals (97 per cent) receiving refunds have a taxable income below $87,000.

More than half of all refunded franking credits are paid to individuals who earn less than the $18,200 tax free threshold.

- More than half of the **number** of individuals receiving a franking credit refund have a taxable income below the tax free threshold, in **value** terms this is around 20 per cent ($500m of $2,200m). Note $5.9 billion is refunded across all entity types.

Regards

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s 22

s 22

From: Brine, Matthew
Sent: Tuesday, 13 March 2018 11:50 AM
To: Gaetjens, Philip; Antioch, Gerry
Cc: s.22(1)(a)(ii) s.22(1)(a)(ii) Fraser, John (Secretary); Mrakovcic, Maryanne; Brennan, Michael; McCullough, Paul; Jeremenko, Robert; s.22(1)(a)(ii) Dowdell, Michelle; s.22(1)(a)(ii) s.22(1)(a)(ii)
Subject: Refundability of franking credits [SEC=PROTECTED]

Hi Phil and Gerry,

We received a number of requests this morning about the ALP's policy on franking credits and I thought it might be best to come back in one consolidated email with what we have.

s 47C and s 47E(d)

The second document is distributional analysis of franking credits and franking credit refunds. Table 5 shows the number of individuals and average value of franking credits by age and Table 6 shows franking credits refunded by age and taxable income.

The third document provides information on SMSF asset allocations and member demographics. This has been developed using publically available ATO and APRA data.

We also received some specific questions for fact checking from s 22(1)(a)(ii)

- two-thirds of the refunds accrue to tax-free superannuation - correct, our figure is 68 per cent
- of the refunds accruing to super, around 90% of those go to self-managed super - correct, our figure is also 90 per cent

- more than half of the cash refunds go to self-managed super with balances of more than $2.5 million & 82% goes to balances of more than $1 million – incorrect although the ALP may be referring to the proportion of payments to super funds that go to SMSFs, we don't have this figure available

We were also asked for views on how the ALP policy would impact:

- Individuals earning below the tax-free threshold amount (this is dealt with in the distributional analysis paper)
- Individuals in receipt of the government aged pension; (we don't have this to hand – we could do some work but it would take some time)
- SMSF members in retirement phase with a median account balance (we don't have this to hand – we could do some work but it would take some time)

We were also asked about what the costing from ANTS would be today if we were to grow it in line with the maturing superannuation system.

- As discussed with Matt Maloney, due to policy changes subsequent to refundability being introduced the original costing cannot be grown to produce a reliable estimate of what the original decision would cost today. Policy changes to individual tax thresholds/rates and superannuation earnings and contribution limits are likely to have had a large impact on refunds beyond the growth of superannuation balances generally.

Please let me know if there is any aspect of this you would like to discuss further or further analysis you need.

Kind regards, Matt

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The distribution of franking credits

Introduction

The purpose of this note is to provide information about the distribution of franking credits across different types of shareholders, s 22 [redacted]

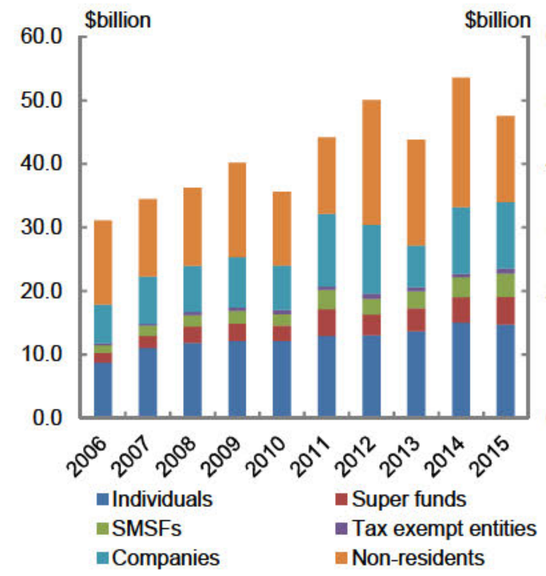
Key points that can be drawn from the analysis include:

- The value of franking credit refunds is growing quickly, and at a much faster rate than distributions of franking credits generally.
- SMSFs are a key driver of growth in franking credit refunds. Two thirds of refunds paid to SMSFs go to SMSFs with average member balances over $1 million.
- The vast majority (85 per cent) of the benefit of franking credit refunds paid to individuals accrues to individuals in the bottom three tax brackets (taxable income below $87,000). Of course, some of these individuals may have high wealth.
- Older Australians are a key beneficiary of refundable franking credits (even before considering refunds to tax free SMSF accounts) suggesting the cost of refundability may increase as the population ages. Further work in this area is desirable.

Franking credit recipients

In 2014-15, $47.5 billion of franking credits were attached to dividends paid by companies, compared to $31.1 billion credits in 2005-06.

Figure 1: Franking credits received by entity type



Around 50 per cent of franking credits in 2014-15 were received by resident entities subject to a final assessment on the dividends (individuals, super funds, SMSFs and tax exempt entities[1]) with the remainder received by other companies[2] and non-residents, both of which generally do not pay additional tax or receive refunds on the dividends.

Around 3.2 million individuals received franking credits in 2014-15 with more than 1.1 million receiving a refund. 200,000 SMSFs, 2,200 super funds and 4,600 tax exempt entities also received a franking credit refund in 2014-15.

Table 1: Utilisation of franking credits by number of entities 2014-15

Number of entities	***Individuals***	***Super funds***	***SMSFs***	***Tax exempt entities***
Received franking credits	*3,200,000*	*2,600*	*310,000*	*4,600*
Franking credits used as tax offset[3]	*2,350,000*	*1,300*	*220,000*	*0*
Franking credits refunded[3]	*1,110,000*	*2,200*	*200,000*	*4,600*

Table 2: Number of individuals receiving franking credits by age 2014-15

Age range	***0 - 25***	***26 - 45***	***46 - 65***	***> 65***
Number of individuals	*110,000*	*800,000*	*1,500,000*	*790,000*

In 2014-15 around 70 per cent of the individuals receiving franking credits were over the age of 45. Similarly, 70 per cent of individuals had a taxable income below $87,000 (this does not include tax free income from superannuation). However in value terms more than 70 per cent of franking credits received by individuals are by those in the top two tax thresholds.

Table 3: Individuals franking credits received by taxable income 2014-15

Taxable income	***Number of individual taxpayers***	***Number receiving credits***	***Franking credits received ($ million)***
Less than $18,200	*2,500,000*	*610,000*	*500.0*
$18,201 - $37,000	*3,100,000*	*610,000*	*1,000.0*
$37,001 - $87,000	*5,400,000*	*1,150,000*	*2,600.0*
$87,001 - $180,000	*1,800,000*	*620,000*	*3,600.0*
Greater than $180,000	*400,000*	*210,000*	*7,000.0*

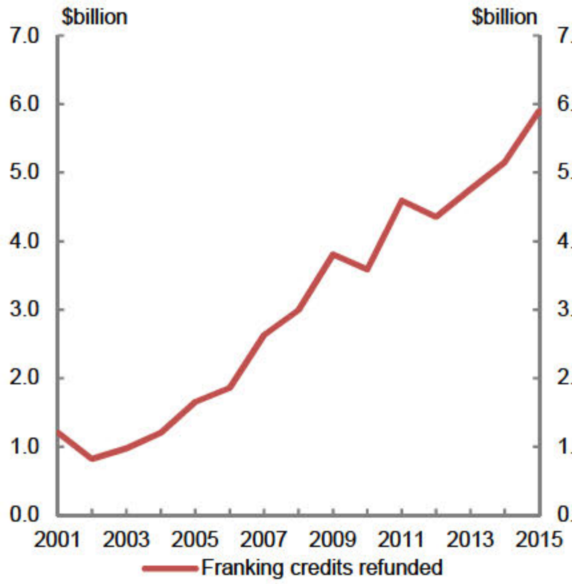
[1] Tax exempt entities include charities, not-for-profit organisations and the Future Fund, which receives the majority of franking credit refunds in this category.
[2] Franking credits received by companies are treated as non-refundable tax offsets and also retained in franking account balances for further distribution.
[3] Depending on tax rates, income from other sources and other available offsets a portion of an entity's franking credits may be used to offset tax liabilities with remaining credits refunded i.e. these categories are not exclusive.

Franking credits refunded

The refundability of franking credits allows a refund of excess franking credits for entities whose tax liability has been reduced to zero. Providing refundability of franking credits allows taxpayers with a marginal tax rate below the company tax rate to receive a refund of tax paid by the company. This means, in effect, that the tax paid by the company is equal to the marginal tax rate of the taxpayer. In the absence of refundability, the taxpayer would, in effect, still pay tax at the company rate with any surplus franking credits wasted.

The value of franking credits refunded has increased significantly over the last decade, from $1.9 billion in 2005-06 to $5.9 billion in 2014-15. While some of this increase is a reflection of the growth in franked dividends paid, personal income tax reductions and the tax exemption of superannuation earnings in pension phase accounts introduced in 2007-08 are likely to have contributed to the increase.

Figure 2: Franking credits refunded

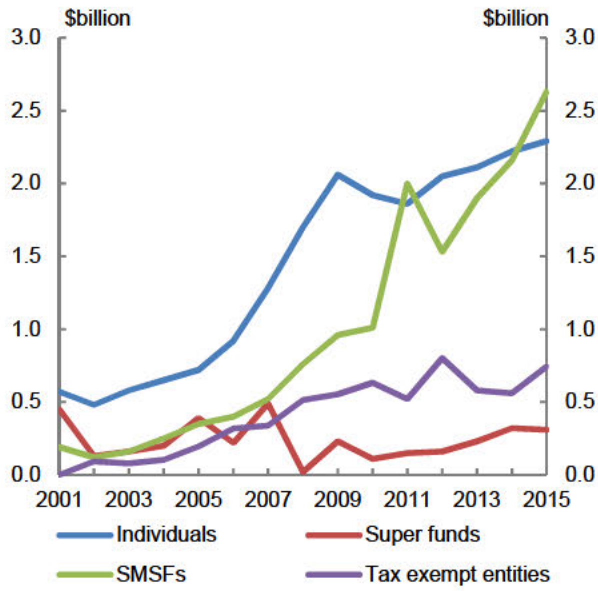


In 2014-15 SMSFs were refunded $2.6 billion in franking credits, followed by individuals ($2.3 billion) tax exempt entities ($0.7 billion) and super funds ($0.3 billion).

The composition of entities receiving refunds has changed significantly since 2005-06 where most refunds were paid to individuals ($0.9 billion) with only $0.4 billion refunded to SMSFs. Subsequent policy changes to retirement earnings in addition to the increasing use of SMSFs as a savings vehicle are likely to be responsible for this change in composition.

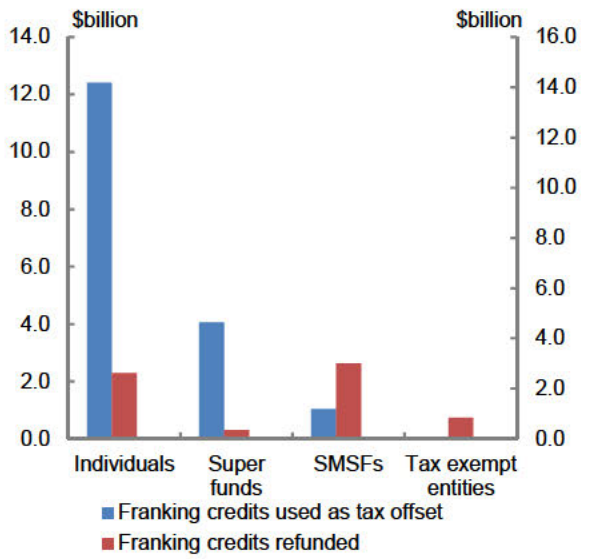
While super funds receive a significant number of franking credits (more than SMSFs) they account for only a small amount of the value of total refunds, as shown in Figure 4. Super funds generally use most franking credits to offset tax on other income sources, including member contributions (i.e. franking credits make up only a small proportion of funds' total taxable income).

Figure 3: Franking credits refunded by entity type



Although each franking credit can only be claimed as a tax offset or a refund, an entity's utilisation may be split in cases where it receives more franking credits than its remaining tax liability. Franking credits will first be used as a tax offset against any outstanding tax liability, with credits in excess of the tax liability being refunded.

Figure 4: Utilisation of franking credits 2014-15[4]



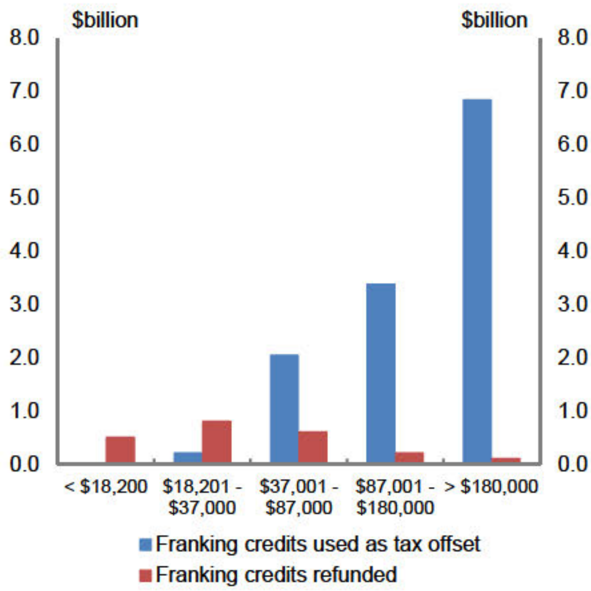
[4] Depending on tax rates, income from other sources and other available offsets a portion of an entity's franking credits may be used to offset tax liabilities with remaining credits refunded i.e. these categories are not exclusive.

In aggregate, individuals also use most of the franking credits received to offset tax liabilities rather than being paid refunds. Refunds to individuals are concentrated within the first three tax brackets (taxable income below $87,000), with $1.9 billion in refunds representing more than 85 per cent of franking credit refunds paid to individuals. This includes around $500 million in refunds to individuals below the $18,200 tax free threshold[5].

Table 4: Franking credits refunded by taxable income ranges 2014-15

Taxable income	***Number of individuals***	***Franking credits refunded ($ million)***
Less than $18,200	*610,000*	*500.0*
$18,201 - $37,000	*360,000*	*800.0*
$37,001 - $87,000	*120,000*	*600.0*
$87,001 - $180,000	*30,000*	*200.0*
Greater than $180,000	*5,000*	*100.0*

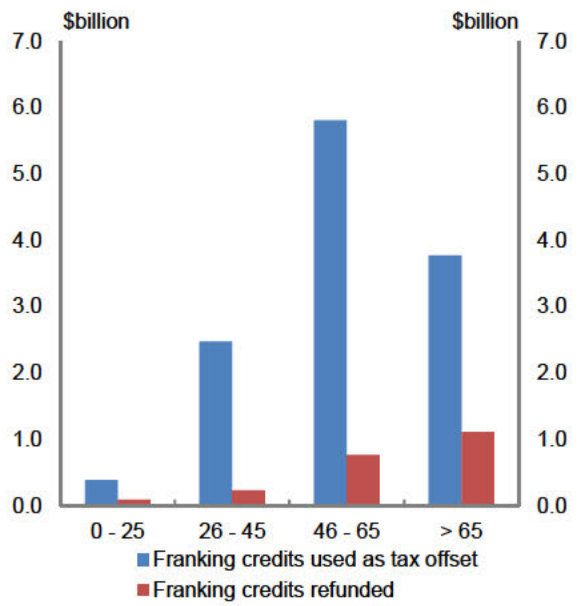
Figure 5: Franking credits utilisation of individuals by taxable income ranges 2014-15[6]



Individuals in the top two tax brackets receive a small amount of overall refunds due to high marginal tax rates. Refunds in these brackets would be limited to individuals with only a small proportion of income from other sources or a significant amount of tax losses/non-refundable tax offsets available.

In terms of age, individuals over 65 were paid around half ($1.1 billion) of franking credit refunds to individuals, with more than 20 per cent of franking credits received being refunded, compared with an average of around 15 per cent for all individuals.

Figure 6: Franking credits utilisation of individuals by age ranges 2014-15



Around 1.1 million individuals received a franking credit refund in 2014-15 with more than half of these over the age of 65.

Table 5: Number of individuals and average value of franking credits by age 2014-15

Age range	***0 - 25***	***26 - 45***	***46 - 65***	***> 65***
Count of individuals				
Franking credits used as tax offset	80,000	710,000	1,250,000	310,000
Franking credits refunded	50,000	120,000	360,000	580,000
Resident population	*7,980,000*	*6,720,000*	*5,530,000*	*3,570,000*
Franking credits refunded as a per cent of population[7]	*0.6%*	*1.8%*	*6.5%*	*16.2%*
Value of franking credits ($ million)				
Franking credits used as tax offset	*400.0*	*2,500.0*	*5,800.0*	*3,800.0*
Franking credits refunded	*100.0*	*250.0*	*750.0*	*1,100.0*

[5] Individuals earning up to the effective tax free threshold (including the low income tax offset) of $20,542 would receive a full refund of franking credits. The seniors and pensioners tax offset also increases the effective threshold.

[6] Individuals with a high taxable income around $180,000 or more are receiving a franking credit refund largely in two situations. Firstly, where they are able to apply losses to dividend income to reduce their taxable income while maintaining full use of franking credits received and secondly where they have a large amount of other non-refundable offsets such as foreign income tax offsets to reduce their tax liability below the amount of franking credits received.

[7] Individuals receiving a refund as a proportion of total Australian population in each age category (ABS cat. no. 3101.0 Australian resident population as at June 2015. 'Resident' is the ABS definition (not tax resident definition).

The number and value of refunds to individuals over the age of 65 is likely driven by a combination of a higher effective tax free threshold through the seniors and pensioners tax offset (SAPTO) and a higher proportion of taxable income received as franked dividends (and lower proportion from other sources such as salary and wages).

Table 5 shows that despite individuals aged over 65 accounting for the highest proportion of franking credit refunds to individuals, the amount of refunds to over 65 year olds is driven by the large number of individuals receiving a refund rather than the amount refunded per person. Furthermore, the 580,000 individuals over 65 receiving a refund account for more than 16 per cent of the 3.6 million Australian residents over the age of 65. This proportion may be even greater if holders of retirement phase accounts in SMSFs receiving refunds are taken into account, although there are difficulties estimating this population in tax data. By comparison a much smaller proportion of the population at younger ages receive franking credit refunds.

Table 6: Franking credits refunded by age and taxable income

($ million)	***0 - 25***	***26 - 45***	***46 - 65***	***> 65***
Less than $18,200	*15.0*	*40.0*	*150.0*	*250.0*
$18,201 - $37,000	*25.0*	*50.0*	*220.0*	*500.0*
$37,001 - $87,000	*40.0*	*80.0*	*250.0*	*250.0*
$87,001 - $180,000	*10.0*	*50.0*	*100.0*	*50.0*
Greater than $180,000	*5.0*	*15.0*	*50.0*	*50.0*

As shown in Table 6, most of the refunds flowing to individuals with a taxable income below $37,000 are to those over the age of 65.

Table 7: Utilisation of franking credits by number of member accounts 2014-15[8]

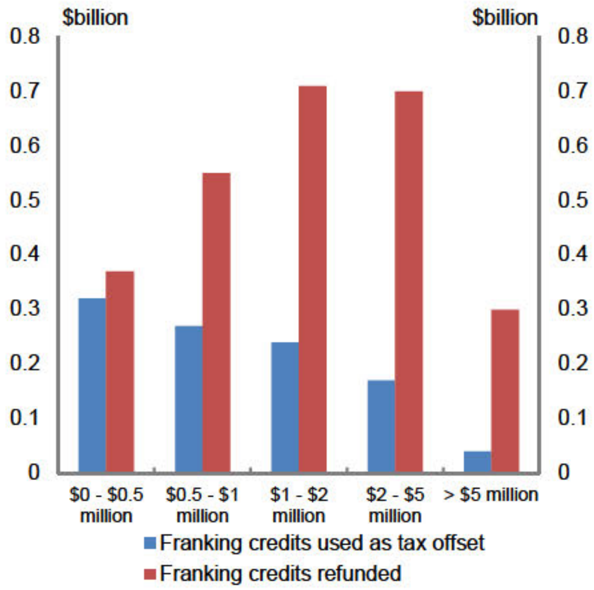
Super fund and SMSF members	***Super funds***	***SMSFs***
Franking credits used as tax offset (fund)	*19,000,000*	*420,000*
Franking credits refunded (fund)	*3,500,000*	*370,000*

While super funds (and SMSFs) are assessed on tax at a fund level, further insight can be provided by the number of member accounts of the funds receiving franking credits.

The 1,300 super funds using franking credits as a tax offset hold 19 million member accounts while the 2,200 super funds receiving a franking credit refund hold 3.5 million member accounts. It is likely that funds receiving a franking credit refund have fewer members in the accumulation phase, and therefore have fewer contributions for the franking credits to offset.

Figure 7 looks more closely at franking credits at the SMSF level, more than two thirds of refunds to SMFSs are to those whose fund balance per member is greater than $1 million. Conversely, SMSFs with an average balance below $1 million account for more than 50 per cent of franking credits used as a tax offset. Given the flat rate of tax on SMSFs, this disparity suggests high wealth funds are more likely to be in the tax-free pension phase (not unexpected as wealth builds over time), have fewer taxable contributions and/or a lower proportion of (unfranked) income from other investments. From 2017-18 the introduction of a balance transfer cap and transition to retirement income changes may reduce this imbalance somewhat as existing earnings are subject to higher tax, resulting in a greater use of franking credits as an offset.

Figure 7: Franking credit utilisation of SMSFs by average member balance[9]



s 47C and s 47E(d)

[redacted]

[8] The number of member accounts will be greater than the number of unique individuals and refers to the number of accounts managed by super funds and SMSFs. Individuals may hold multiple accounts across different funds, with each account counted in the table.

[9] The average member balance of an SMSF is its total member account balance divided by the number of members.

SMSF Factsheet

- As at September 2017, there were 598,620 SMSFs and 1,130,721 total members of SMSFs.
- The table below contains an approximate age distribution of individuals who were members as at the end of June 2017.

Table 1: Member demographic table

Age range	Male	Female	Total
<25	0.7%	0.7%	0.7%
25–34	3.7%	3.9%	3.8%
35–44	11.8%	13.0%	12.4%
45–49	10.1%	11.1%	10.6%
50–54	11.5%	12.4%	11.9%
55–59	13.4%	14.1%	13.7%
60–64	13.4%	14.1%	13.7%
65–69	13.6%	13.5%	13.6%
70–74	11.2%	9.8%	10.5%
75–84	9.4%	6.7%	8.1%
85+	1.4%	0.7%	1.1%
Unknown	0.0%	0.0%	0.0%
Total	100.0%	100.0%	100.0%
All ages	52.6%	47.4%	100.0%

- This table below contains an approximate distribution of the taxable income of individuals who were SMSF members as at the end of June 2017.

Table 2: Member demographic table – income ranges

Income ranges	Male	Female	Total
$0–$20,000	19.1%	25.7%	22.2%
>$20,000–$40,000	16.1%	21.3%	18.5%
>$40,000–$60,000	11.1%	14.0%	12.5%
>$60,000–$80,000	10.8%	10.8%	10.8%
>$80,000–$100,000	8.6%	7.3%	8.0%
>$100,000–$150,000	12.4%	7.8%	10.2%
>$150,000–$200,000	7.5%	4.7%	6.2%
>$200,000–$500,000	8.3%	3.7%	6.1%
>$500,000	2.5%	0.9%	1.7%
Unknown	3.6%	4.0%	3.8%
Total	100.0%	100.0%	100.0%

Asset allocations

- Due to differences in reporting requirements and timing of data releases, the below asset allocations for SMSFs and APRA funds are broken down in different ways and are not directly comparable to each other.

- The table below outlines SMSF asset allocations as estimated at September 2017.

Table 3: SMSF asset allocations

	$ million	Per cent of total Australian and overseas assets
Listed trusts	32,834	4.7
Unlisted trusts	74,724	10.7
Insurance policy	111	0.01
Other managed investments	37,684	5.4
Cash and term deposits	158,071	22.5
Debt securities	9,683	1.4
Loans	4,459	0.6
Listed shares	206,231	29.4
Unlisted shares	7,054	1.0
Limited recourse borrowing arrangements	30,730	4.4
Non-residential real property	79,131	11.3
Residential real property	33,795	4.8
Collectables and personal use assets	330	0.05
Other assets	17,974	2.6
Overseas shares	4,588	0.6
Overseas non-residential real property	142	0.02
Overseas residential real property	292	0.04
Overseas managed investments	838	0.1
Other overseas assets	2,933	0.4
Total Australian and overseas assets	**701,604**	
Borrowings	**22,851**	**3.3**
Other liabilities	**6,037**	**0.9**
Total net Australian and overseas assets	**672,716**	

Source: ATO's SMSF statistical report

- The table below outlines the entities with more than four members' asset allocations as estimated at December 2017.

Table 4: Superannuation industry asset allocations of entities with more than four members

	$ million	Per cent of total investments
Cash	179,593	11
Australian fixed income	207,311	12.7
International fixed income	127,465	7.8

Australian listed equity	383,156	23.4
International listed equity	390,731	23.9
Unlisted equity	66,881	4.1
Listed property	52,055	3.2
Unlisted property	82,741	5.1
Listed infrastructure	21,788	1.3
Australian unlisted infrastructure	38,090	2.3
International unlisted infrastructure	21,121	1.3
Commodities	1,678	0.1
Other	58,701	3.6
Total investments	**1,633,978**	

Source: December 2017 APRA Quarterly Superannuation Performance Statistics.

From: Maloney, Matthew
To: s 22(a)(ii)
Cc: Mrakovcic, Maryanne; Gaetjens, Philip; RG TAD SES; s 22(a)(ii) ; Jeremenko, Robert
Subject: Refundable Imputation - Pensioner Numbers [SEC=PROTECTED]
Date: Tuesday, 13 March 2018 7:14:41 PM

Hi s 22(a)(ii)

Just getting back to you on the pensioner question you asked.

Using the labels available to us on the 2014-15 individual tax return we have been able to estimate that around 230,000 pensioners would be affected by the policy to deny the refund of imputation credits. That is around 20 per cent of the affected population of 1.1 million. By value this is worth around $300m of the $2,200 million refunded to individuals.

Please note that the label we use would include recipients of the age pension, the disability support pension and a small amount of the carer payment.

Let me know if you need anything further.

Regards

Matthew Maloney
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Subject: FW: Refundability of franking credits [SEC=PROTECTED]
Attachments: Refundability of franking credits - Original costing.docx

Hi again Phil and Gerry,

Just an update on where we are up to with the work on refundability of franking credits.

On Phil's question below about the growth in cost of imputation, we've prepared a short note on what we see as the main drivers of growth (attached). In short, while growth in the economy and superannuation assets explains part of the story we think that policy changes after the introduction of refundability were significant drivers of the cost increase.

s 22 [redacted]

We received a request from s.22(1)(a)(ii) about the number of pensioners affected and Matt Maloney sent this through a few minutes ago. Using the labels available to us on the 2014-15 individual tax return we have been able to estimate that around 230,000 pensioners would be affected by the policy to deny the refund of imputation credits. That is around 20 per cent of the affected population of 1.1 million. By value this is worth around $300m of the $2,200 million refunded to individuals. Please note that the label we use would include recipients of the age pension, the disability support pension and a small amount of the carer payment.

s 22 [redacted]

Kind regards, Matt

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- two-thirds of the refunds accrue to tax-free superannuation - correct, our figure is 68 per cent
- of the refunds accruing to super, around 90% of those go to self-managed super - correct, our figure is also 90 per cent
- more than half of the cash refunds go to self-managed super with balances of more than $2.5 million & 82% goes to balances of more than $1 million – incorrect although the ALP may be referring to the proportion of payments to super funds that go to SMSFs, we don't have this figure available

We were also asked for views on how the ALP policy would impact:

- Individuals earning below the tax-free threshold amount (this is dealt with in the distributional analysis paper)
- Individuals in receipt of the government aged pension; (we don't have this to hand – we could do some work but it would take some time)
- SMSF members in retirement phase with a median account balance (we don't have this to hand – we could do some work but it would take some time)

We were also asked about what the costing from ANTS would be today if we were to grow it in line with the maturing superannuation system.

- As discussed with Matt Maloney, due to policy changes subsequent to refundability being introduced the original costing cannot be grown to produce a reliable estimate of what the original decision would cost today. Policy changes to individual tax thresholds/rates and superannuation earnings and contribution limits are likely to have had a large impact on refunds beyond the growth of superannuation balances generally.

Please let me know if there is any aspect of this you would like to discuss further or further analysis you need.

Kind regards, Matt

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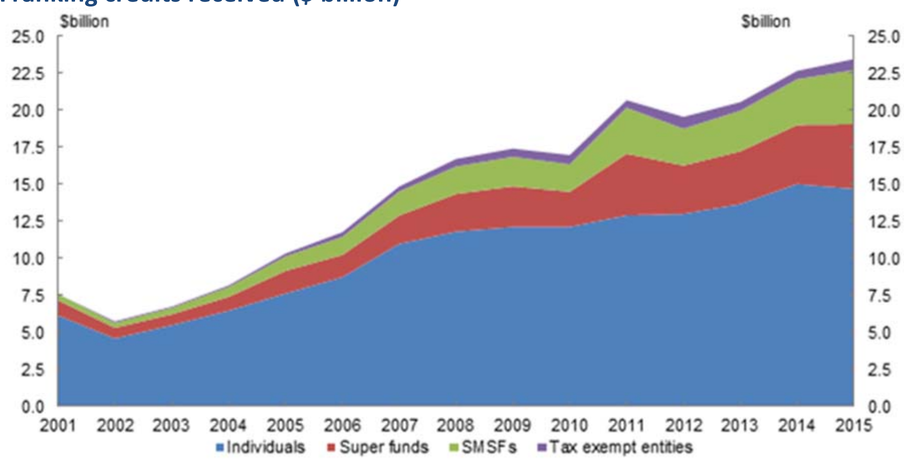
Refundability of franking credits

There has been significant growth in the value of franking credits received by entities eligible for franking credit refunds since the introduction of refundability in 2000-01. Around $7.6 billion in franking credits were received in 2000-01 by the entity types able to receive a franking credit refund. This has tripled over time to around $23.5 billion in 2014-15. The share of franking credits received by superannuation funds has increased from 19 per cent in 2000-01 to 34 per cent in 2014-15.

The introduction of refundability was originally estimated to cost $550 million in 2001-02 (the costing was published in 1998). While there has been significant growth in franking credits received and change in composition towards superannuation funds this alone is unlikely to be the driver of the increase in refunds.

- While the number of franking credits received by APRA funds has increased more than four times, since 2000-01, the number of credits refunded has actually fallen.
- Before the introduction of tax free retirement earnings in 2007-08 on average around 35 per cent of credits received by SMSFs were refunded. Since 2007-08 this averages 60 per cent.
    - For individuals the average was around 10 per cent before 2006-07 (before significant income tax cuts), increasing to 15 per cent since.

Franking credits received ($ billion)



Share of franking credits received (entities eligible for refunds only)