



THE TAX INSTITUTE

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Mr Mark Sewell
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The Treasury
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Dear Mr Sewell

Discussion Paper - Proposed Amendments to the Corporations Act

The Tax Institute is pleased to make the following submission in response to Treasury's Discussion Paper entitled "Proposed Amendments to the Corporations Act" (the "**Discussion Paper**").

We note that the range of taxation issues that have arisen from the recent and proposed reforms (as set out on page 11 of the Discussion paper) have resulted in significant uncertainty for a range of taxpayers. As such, we strongly urge implementation of reforms necessary to bring this uncertainty to an end.

In this regard we note with disappointment the lack of impetus that appears to belie the discussion in relation to taxation issues in the Discussion Paper. Specifically we note the lack of any proposal in the Discussion Paper to amend the law in order to address these taxation issues.

We encourage consideration of the tax consequences of any proposed reforms, as well as amendment of the existing law to deal with the taxation issues referred to above.

Our detailed submission is as follows.

1. Uncertainty for taxpayers regarding franking dividends

As noted in the Discussion Paper, there is significant uncertainty in relation to whether dividends paid in accordance with the revised section 254T of the Corporations Law 2001 may be franked. In this regard, the Australian Taxation Office' ("**ATO**") has recently issued Draft Taxation Ruling TR 2011/D8 ("**Tax Ruling**"). The Tax Institute will provide comments on the Tax Ruling to the ATO.

2. Option 4 should be adopted

2.1. The Tax Institute recommends that Option 4 be adopted as it provides the most flexibility for taxpayers. Option 4 would give directors some comfort that, where a dividend is paid out of profits, it will be a frankable dividend for tax purposes. It is recommended that if Option 4 is adopted, a definition of profits is also inserted (see part 3 below).

2.2. However, if Option 2 is adopted (the solvency test), The Tax Institute recommends that an alternative profits test is also available, for the reasons in paragraph 2.1 above. If an alternative profits test is not adopted, the solvency test would give rise to the same concerns raised by taxpayers and the ATO in relation to current section 254T (which are discussed on page 11 of the Discussion Paper).

3. Insert definition of profits

3.1. A definition of “profits” should be inserted into the Corporations Act. The Discussion Paper states on page 8 that the profits-based dividends test is easy to understand. However, the Discussion Paper also provides on page 7 that one of the problems with the profits test is that the lack of a definition of, or guidance about, the term profits creates confusion.

3.2. The joint opinion provided to the ATO on the operation of section 254T that was recently given by A H Slater and J O Hmelnitsky dated 29 November 2011 (refer <http://law.ato.gov.au/pdf/pbr/ato254tadvicefinal1211.pdf>) (“**Tax Opinion**”) refers to the case law on the definition of profits (refer page 13). The Tax Institute recommends adopting that definition:

Profits means profits as disclosed by accounts prepared in accordance with the requirements of the Corporations Act.

3.3. Similarly, a definition of assets and liabilities should be inserted to reduce confusion.

4. The Treasury’s interpretation of section 254T conflicts with the ATO’s interpretation

4.1. The ATO’s interpretation of section 254T appears to differ from the Treasury’s approach. The ATO takes the view that, “section 254T does not authorise any act by a company; the section merely prohibits the payments of dividends in the specified circumstances” (refer paragraph 16 of the Tax Ruling). The ATO has relied on the Tax Opinion in reaching this conclusion.

4.2. The Treasury’s approach in the Discussion Paper, however, indicates that section 254T is a permissive power. For example, Option 4 appears to be intended to give a company two positive choices for determining whether it could pay a dividend.

4.3. On the ATO’s reading of section 254T, Option 4 would create two limitations on when a dividend could be paid.

4.4. Accordingly, if Option 4 is to be adopted, the new section 254T would need to be drafted as one test being an exception to the other test. For example:

A dividend may only be paid out of profits.

Despite section 1, a company will not be prohibited from paying in dividend if:

[insert 254T language]

4.5. The ATO should be party to the design of these provisions to ensure that there are no unintended tax consequences and that there is a common understanding of the intended interpretation and application of these rules.

5. Other matters – enactment of new “qualified persons” legislation

A further area of confusion and complexity for taxpayers is the application of the former “qualified person” rules in the *Income Tax Assessment Act 1936*. These rules were repealed in 2002 but still apply to taxpayers (refer to Taxation Determination TD 2006/D40 for a discussion of this issue.)

Taxpayers apply the law on the basis that the rules will be re-enacted in substantially the same form. The enactment of such rules, as announced by the Treasurer on 13 May 2008, would make the tax treatment of dividends more certain. Additionally, this would also present the opportunity to legislate the recommendations (which were adopted by the then government) following the Review of Business Taxation report.

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If you would like to discuss this matter, please contact me on (02) 8223 0011 or The Tax Institute’s Tax Counsel, Deepti Paton on (02) 8223 0044.

Yours sincerely



Ken Schurgott
President