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Tax White Paper Task Force

The Treasury
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Australian Taxation System Dividend Imputation System

Submission

This submission relates to the maintenance of our current dividend imputation system.

Dividend Imputation System

As part of the review of Australia's taxation system it is important that we **maintain** the current dividend imputation system. This system has significant benefits to our corporations, retail investors, those with superannuation and pension schemes and to the Australian Taxation Office.

Some of the reasons to maintain our dividend imputation system are:

1.It eliminates the double taxation of dividends

Prior to the introduction of the dividend imputation system the profits of a corporation were taxed twice.

- Firstly if a corporation made a profit of \$100, tax was paid to the Australian Taxation Office (ATO) at the corporate rate of 30%, ie \$30 is paid to the ATO.
- If the remainder of the profit was paid as a dividend to its shareholders the dividend would be taxed at the shareholders marginal tax rate eg 47%, $70 \times 47\% = \$32.90$
- That is, of the profit \$100.00, \$62.90 is paid in tax, only \$37.10 remains untaxed. Note, this is excluding the Medicare Levy.

The company profits have in effect been taxed twice.

The current system by providing an imputation credit to the shareholder means that the shareholder is obtaining the benefit of the tax paid by the company, the ATO is in effect still collecting their share of tax from the individual, ie on a look through basis of 47%. There is no double taxation of dividends.

To reintroduce the double taxation of dividends would catastrophic to the small business sector in particular, it would eliminate the incentive to seek a higher income and advance oneself.

2.It encourages corporations to pay company tax.

Prior to the introduction of the dividend imputation system some corporations would engineer the way that certain transactions were done (eg sometimes involving tax havens) to achieve a certain outcome which meant that a lower amount of tax was paid to the ATO.

With the introduction of dividend imputation corporations were encouraged by their shareholders to be good corporate citizens by paying income tax to the ATO. Shareholders were well aware of the benefits of receiving a franked dividend, this created some pressure/encouraged corporations to pay their share of income tax so they could pay a franked dividend.

This created a win - win situation where the corporations, shareholders and the ATO were all winners. The encouragement to pay income tax via the dividend imputation system is far more effective than any 'heavy handed approach' by the ATO.

3.It provided a greater source of capital for our corporations.

As investors became aware of the benefits of the dividend imputation system it encouraged some investors who previously did not invest in share capital, to buy shares in corporations with the intention of receiving a franked dividend. Those investors who already held some shares were more willing to provide additional capital to existing or new corporations.

Without capital corporations cannot operate, the Australian economy requires corporations to provide goods and services. These corporations then require employees to carry out various functions and hence provide employment to Australians.

Hence, the dividend imputation system has provided a greater source of capital for our corporations. Any tinkering with our dividend imputation system will reduce the amount of available capital to our corporations and the negative consequences for our country.

If capital can be generated domestically it has a lower cost to the country as any foreign capital will need to be serviced which then generates an outflow of funds from this country.

Also, an Australian company will still proceed with a foreign investment (regardless of dividend imputation) providing the returns and risks meet various benchmarks set by the board of directors.

Please feel free to contact me if you wish to discuss any of the issues that I have raised in this submission.

Yours faithfully

Jonathan Hestelow