Director
Corporate Tax Policy Unit
Treasury
Langton Cres
Parkes ACT 2600

By email: frankeddistconsult@treasury.gov.au

Dear Director,

Thank you for the opportunity to submit a response to the consultation on the proposed legislation relating to Franked Distributions and Capital Raising.

I object to the proposed legislation changes because I think they are confused, incomplete, a response to a problem that doesn't exist, and unfair to Australian shareholders who have made decisions in good faith based on the existing legislation. The proposed changes could also inadvertently compromise legitimate equity raisings.

The draft legislation fails to recognise the fundamental principle underlying the franking regime and the reason for its creation: the avoidance of double taxation on company earnings. The Franked Distribution and Capital Raising draft legislation, if widely applied, will lead to the demise of the franking system. It will stop Australian companies which issue new shares under a Dividend Reinvestment Plan (DRP) from paying franked dividends and significantly increase the cost of capital for all Australian companies paying franked dividends. It will also risk the stability and integrity of the Australian banking system by inhibiting effective capital raising during challenging economic periods such as the start of the coronavirus pandemic and the global financial crisis.

If passed, its application would also unfairly burden Australian investors with retrospective tax debts at a time of elevated pressures on their personal cashflows from large increases in the cost of living.

Yours sincerely,

David Walker

Submission

1. There would be unintended consequences based on the current drafting of the proposed legislation. As drafted the proposed legislation does not sufficiently distinguish between acceptable equity raisings and

the tax avoidance it intends to address. The proposed legislation will inadvertently deter legitimate equity raisings and delay and discourage the normal processes of capital raising, investment and economic growth in Australia. It will also interfere with the operation and the efficiency of the Australian capital markets and the structural integrity of our banking system.
For example, in addition to normal and legitimate equity raisings and franked dividend payments by Australian companies, the draft legislation is broad enough that it could also capture the well-established practice of Dividend Reinvestment Plans (DRPs) and underwritten capital raisings in the circumstances where, in Treasury’s broad view, the established practice test is not met.

The current draft of the legislation will severely affect our authorised deposit-taking institutions and contradict the Australian Prudential Regulation Authority's guidance in the most recent time of economic stress during the COVID-19 pandemic. In April 2020 APRA said bank boards should seriously consider deferring dividends given the economic uncertainty created by lockdowns and border closures. As Australia moved beyond the initial phase of response, APRA updated the guidance to assist longer-term capital management enabling banks to fulfil their role in supporting economic recovery. As part of this, APRA recommended they actively used DRPs "and/or other capital management initiatives" to offset the reduction in their capital base and balance sheets from making franked dividend payments to their shareholders. The proposed drafting of the legislation changes will risk the stability of the Australian banking system by inhibiting effective capital management during challenging economic times.

2. Managing cash flows between capital raising and distributions can represent the normal and legitimate flow of commercial capital management The drafted legislation removes the ability of operating businesses to legitimately manage and invest their cash flows productively. Once a company has generated a profit and reinvested it, it can only create liquidity to pay a dividend by raising debt, selling some of its assets (which might not be viable) or by raising capital. By removing the ability to raise capital to reward shareholders, companies will need to increase their debt levels or they will be put in a position where they will be unable to grow and further develop their businesses. While there are instances of companies manipulating the tax system, companies that have legitimately earned profits and paid tax should be entitled to choose how they invest or distribute those profits to their shareholders.

3. The proposed legislation would burden thousands of Australian shareholders who have planned or are planning their retirement, placing stress on individuals and on the Australian pension system. The dividend imputation system has not fundamentally changed for over 20 years and implementing change now, and retrospectively, on people who are already retired and, in many cases, cannot return to work, will burden individuals, their families and in turn the economy, all of which will face economic uncertainty.

4. The retrospective application to 19 December 2016 would unfairly prejudice franked dividends paid out to shareholders of Australian companies and leave them with unexpected tax bills for dividends they have since received, to be paid at a time of economic uncertainty. This is particularly concerning for those who rely on fully franked dividends as income. Those shareholders relied on the existing franking legislation in years back to 2016 and it would be extremely unfair to penalise them for acting in good faith at the time. Many also simply could not afford to pay back taxes. Tax laws should not be allowed to change retrospectively when Australians have budgeted for and paid their lawful tax assessment based on existing tax law in place.

The proposed legislation, as drafted, will fundamentally change the nature of how Australian companies manage their capital, increase their cost of capital and disadvantage Australian shareholders. I call on you to abandon the legislation.