CHARTERED ACCOUNTANTS™
AUSTRALIA + NEW ZEALAND

2 November 2018

The Committee Secretary
Standing Committee on Economics
PO Box 6021
Parliament House
Canberra ACT 2600

Submission lodged via email to: economics.reps@aph.gov.au

Dear Sir or Madam

Inquiry into the implications of removing refundable franking credits

Chartered Accountants Australia and New Zealand welcomes the opportunity to provide a submission to the Standing Committee on Economics for its Inquiry into the implications of removing refundable franking credits. For consistency, our submission uses the term "franking tax offsets" rather than "franking credits".

Appendix A provides our detailed submission, Appendix B shows relevant data from the Parliamentary Budget Office and Appendix C provides more information about Chartered Accountants Australia and New Zealand.

The political context

In writing this submission we have endeavoured to provide the Committee with insights that address the Terms of Reference in a dispassionate way, ignoring the looming Federal Election and the political contest that will occur around the Australian Labor Party's announced policy of limiting the refundability of excess franking tax offset entitlements.

That said, many Chartered Accountants in public practice in Australia have expressed to us their concerns about the impact the ALP's proposal would have on their clients. Their insights are reflected in this submission.

Key concerns

Feedback from our members is that any decision to remove refundability will result in predictable and quite legitimate behavioural adjustments to investment strategies to maximise franking tax offset *utilisation*. Members are therefore highly sceptical of revenue projections for this measure.

However, the removal of refunds is expected to have a substantial disadvantageous impact on:

- Self-funded retirees whose personal circumstances – or the circumstances of the superannuation or investment fund to which they belong – make it difficult to establish new assessable income streams which *utilise* excess franking tax offset capacity (as distinct from *refunding* the excess).

Chartered Accountants Australia and New Zealand
33 Erskine Street, Sydney, NSW 2000
GPO Box 9985, Sydney NSW 2001 T +61 2 9290 1344

GAA Global Accounting Alliance
Chartered Accountants Worldwide

- Low income earners deriving small amounts of franked dividends.

There is also a sizeable group of clients who have based their *future* retirement and investment plans on the continued availability of refunds.

Both client groups – those currently receiving refunds and those who have planned to – regularly convey to their Chartered Accountant exasperation at the uncertainty caused by unexpected changes to income tax and superannuation policy settings which to date appeared to have enjoyed bi-partisan political support.

Committee members should be under no misapprehension: there is growing community distrust in tax and superannuation policy decision-making.

Piecemeal changes which gradually erode entitlements, justified on the basis that they impact only a privileged few, are increasingly being called-out by clients as opportunistic, misrepresented to the community, and indicative of the unwillingness or inability of the political class to engage with Australians about the broader tax reforms necessary to create a sustainable tax base.

Chartered Accountants are also starting to express concern about possible implementation issues should franking tax offset refundability be curtailed.

Data

It is very important for the Committee's deliberations to be informed by the best data obtainable from the ATO, Treasury, the ASX and other organisations (such as the Parliamentary Budget Office). For example, it would be useful to know the amount of unutilised franking credits currently in the franking accounts of Australian companies and the extent to which franking tax offset refunds are currently paid and expected to be paid in the future.

The Committee needs a detailed profile of those who currently receive refunds.

If the policy justification is that curtailing refunds impacts mainly "wealthy" taxpayers, supporting data should also be obtained and scrutinised. On this point, we would also ask the Committee to note that Australia has a progressive *income* tax system, and that using this system to target *wealth* (as distinct from income) is a much broader discussion which will take the Committee far beyond its current terms of reference.

At a macroeconomic level, we also think it is important for the Committee to obtain the best data it can about the impact which refundability has had on dividend pay-out ratios, Australian (tax) resident company decision-making on the jurisdiction in which company income tax is paid and dividend pay-outs, and investor preference for shares yielding franked dividends.

Importantly, the Committee should seek expert insights about the likely secondary effects of removing refunds.

Further input

We look forward to participating further in the Committee's consultations process and consent to the publication of this submission.

Should you have any queries concerning the matters discussed in our submission or wish to discuss them in further detail, please contact Michael Croker

Yours sincerely,

Michael Croker CA
Australian Tax Leader
Advocacy & Professional Standing
Chartered Accountants Australia and New Zealand

Appendix A

1. A brief excursion into the history of dividend imputation

Under the imputation system, Australia's company income tax system operates as a withholding tax on the income Australian residents earn through Australian resident companies, and as a final tax on (primarily Australian source) income earned by non-residents through an Australian resident company or permanent establishment in Australia.

Australia has a progressive Federal income tax system and a consumption tax. It does not have an explicit wealth tax. Having refundable franking credits supports the progressive income tax system by ensuring the taxpayers have tax imposed at their marginal tax rate. Providing a refund of a franking credit to individuals is effectively the same as providing a refund for PAYG withholding – it merely represents the tax withheld by a company in anticipation of a resident individual's taxable income calculation.

A franking tax offset refund is not a repayment of tax that has not been earned. The shareholder has borne risk and made a significant contribution of assets to generate the dividend and associated franking credit.

However, refundable franking tax offsets were deliberately not part of the original dividend imputation policy or legislative design[1].

This partly explains why, on 19 September 1985, the then Treasurer Paul Keating said the introduction of dividend imputation would only cost the revenue $250 million annually (bearing in mind that he also increased the company tax rate from 46% to 49% that day, thereby aligning the company tax rate with the top personal marginal rate)[2].

Treasury officials at the time envisaged that a sizeable proportion of franking credits would be "wasted" (unutilised)[3]. For example, the imputation system was designed so that the only benefit foreign shareholders obtained from franked dividends was an exemption from dividend withholding tax. But the main means of ensuring wastage was to deny refunds for any excess franking offsets.

However, the value of franking tax offset entitlements soon came to be well understood.

The so-called "clientele effects" predicted at the time dividend imputation was introduced were quickly observed in practice. These mainly took the form of tax and financial planning which sought to place franking tax offset entitlements into the hands of those shareholders whose tax profiles meant they gained the maximum after tax benefit.

Various anti-avoidance measures resulted, including:

- Anti-dividend streaming rules[4]
- Anti-capital streaming rules[5]
- Holding period rules (often referred to as the "45 day rule)[6], and
- Imputation rules for exempting and former exempting entities[7]

---

[1] Source:
https://parlinfo.aph.gov.au/parlInfo/search/display/display.w3p;query=Id:%22legislation/billsdgs/MW506%22
[2] Ministerial Statement, 19 September 1985. Source:
https://parlinfo.aph.gov.au/parlInfo/search/display/display.w3p;query=Id:%22chamber/hansardr/1985-09-19/0108%22;src1=sm1
[3] At para 4.6, *Explanatory Memorandum* to the Bill, it is stated that it was intended that some shareholders would be unable to use a franking credit attached to a dividend.
[4] Taxation Laws Amendment Bill (No. 3) 1998.
[5] Taxation Laws Amendment (Company Law Review) Bill 1998.
[6] Taxation Laws Amendment Bill (No 4) 1998, Schedule 4.
[7] Taxation Laws Amendment Bill (No 4) 1998, Schedule 5.

- Enhancements to the general anti-avoidance provision, known as Part IVA[8].

The introduction of refundability in 2000

In 2000, as part of a tax reform package, the law was amended by Prime Minister John Howard's Coalition government to allow franking tax offset refunds[9].

According to the explanation provided at the time[10], the law was changed:

> "to ensure…eligible taxpayers are taxed at their appropriate marginal rates of tax on assessment. As a result, self-funded retirees, and other low income resident individuals, will no longer face an effective rate of tax on their investments in entities greater than their marginal rate. For superannuation funds, the non-refundability of imputation credits can distort investment decisions".

The Australian Labor Party supported the 2000 changes. Indeed, as pointed out at the time by Shadow Treasurer Simon Crean, Labor had taken this policy to the 1998 Federal Election[11]:

> "Although imputation credits can be used to reduce an individual's or a superannuation fund's income tax liability to nil, excess credits were of no value to taxpayers. This bill proposes to refund to taxpayers any excess imputation of credits that may be left after offsetting the credits against their income tax liability.
>
> The classic example of such a situation is a low-income person who earns a little investment income - for example, a full rate age pensioner. They face no income tax liability on their income and therefore cannot obtain the benefit of the excess franking credits attached to the small amount of dividend income they receive.
>
> Under this proposal, they will obtain a refund of their income tax from the Taxation Office, representing the excess imputation credits. Labor included this proposal in our taxation policy prior to the last election.
>
> Therefore we have no difficulty supporting the proposal because it is our policy.
>
> It builds on the major reform accomplished by Labor almost 15 years ago and it improves the current taxation situation faced by low income investors, especially retired Australians."

Other Labor MPs supported the measure "for the people on small incomes - the retirees on fixed incomes from returns on investments and also people on pensions who have got a very small return from investments"[12].

Refundability enhanced by Labor's discretionary trust reforms in 2011

On 4 March 2011, the Minister for Financial Services and Superannuation, Bill Shorten, announced that, in response to the High Court decision in *Bamford v FCT* [2010] HCA 10, "the law will be amended to enable *streaming* of capital gains and franked distributions to [trust] beneficiaries"[13].

---

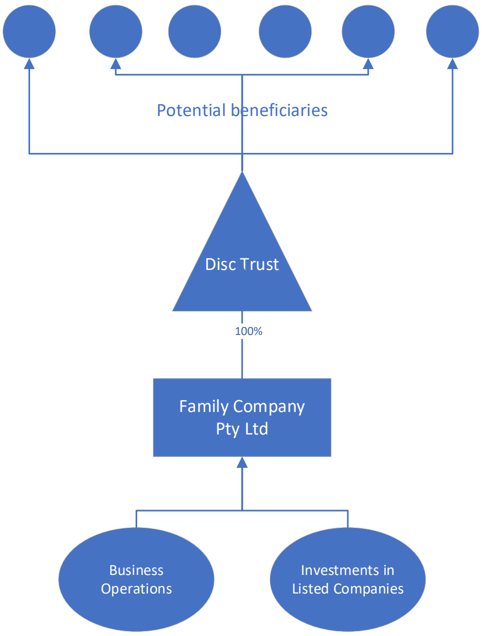
[8] Section 177EA of the Income Tax Assessment Act 1936 targets franking credit trading and dividend streaming schemes where one of the purposes (other than an incidental purpose) of the scheme is to obtain a franking credit benefit.
[9] New Business Tax System (Miscellaneous) Bill 1999. The refundable tax offset rules are now located in Division 67 Income Tax Assessment Act 1997.
[10] Source: http://ministers.treasury.gov.au/ministers/phc/content/PressReleases/1999/attachments/058/M.PDF
[11] Hansard, 17 February 2000, page 13,734. Source: https://parlinfo.aph.gov.au/parlInfo/download/chamber/hansardr/2000-02-17/toc_pdf/173-4969.pdf;fileType=application/pdf
[12] Michael Hatton MP, Labor, Blaxland. Hansard 17 February 2000, page 13,750. Op cit.
[13] Bill Shorten, Assistant Treasurer, Media Release, *Providing Certainty for Trusts*, 4 March 2011. Source: http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=pressreleases/2011/040.htm&pageID=003&min=brs&Year=2011&DocType=0

In a speech delivered the same day, Mr Shorten also said: "We don't believe trusts are any form of tax avoidance. We see trusts as a legitimate feature of how Australians conduct their financial affairs"[14].

Subject to various safeguards and the need for a properly worded trust deed, this announcement effectively allowed discretionary trusts to "stream" franked dividends to those beneficiary profiles where the franking tax offset entitlement was of most value.

The announcement further encouraged the establishment of an investment structure widely used to this day for business and \ or private investment purposes:

Diagram 1: A discretionary trust used in tandem with a private company



Although outside the Committee's Terms of Reference, Chartered Accountants ANZ are, at this stage, unclear about the interplay between Labor's policy to curtail refundability and another of the ALP's announced policies, the 30% minimum distribution tax on discretionary trust distributions[15].

SMSFs and Employee Share Schemes

Two other important historical trends have contributed to growing interest in franked dividends.

- The growth in the number of SMSFs, recorded by the ATO over the five years to 2017 to have increased from 473,000 to 597,000 (26% over the period). SMSF assets grew by $274.3 billion or 65% over the same timeframe[16].

[14] Bill Shorten, Assistant Treasurer, *What We Get for Our Taxes*, Speech to The Taxation Institute, Brisbane, 4 March 2011. Source: http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=speeches/2011/007.htm&pageID=005&min=brs&Year=2011&DocType=1

[15] Australian Labor Party, *A Fairer Tax System. Discretionary trust reform*, 30 July 2017. Source: https://d3n8a8pro7vhmx.cloudfront.net/australianlaborparty/pages/7652/attachments/original/1501324995/170729_Shorten_Trusts_Fact_Sheet_FINAL.PDF?1501324995

[16] ATO website, Growth of SMSF assets, Last modified 18 January 2018. Source: https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Super-statistics/SMSF/Self-managed-superannuation-funds--A-statistical-overview-2015-2016/?page=3

- The use of Employee Share Schemes (ESS). According to one source, the proportion of Australian firms with ESS grew from 0.23 per cent to 0.57 per cent from 2006–07 to 2014–15. Estimated annual ESS payments were $2 billion in 2014–15 accounting for approximately 0.4 per cent of total wages and salaries in Australia[17].

For both types of investment structures, benefits can be obtained from the refundability of excess franking tax offsets.

Further information on SMSFs is provided below.

As for ESS, Committee members should note that franking tax offset entitlements will often flow to employee participants in such schemes, usually via the ESS trust which typically holds the shares for employee members of the scheme. Many Australian workers hold small share parcels under the income-tested $1,000 reduction available under the ESS "taxed-upfront scheme" (effectively enabling eligible employees to receive shares worth up to $1,000 tax free per financial year)[18].

Recommendation

Australia has high levels of direct and indirect share ownership[19].

We ask Committee members to note the bipartisan political support for Australia's dividend imputation system and its development over the years.

Although we are not suggesting that policies should never be re-considered or reversed, the historical context is that:

1. Since 1987, the dividend imputation system has encouraged Australians to invest in Australian companies yielding franked dividends.
2. The introduction of refundability in 2000 was a bipartisan policy decision seen as particularly beneficial to *low income earners and self-funded retirees.* The policy acknowledged the adverse impact non-refundability had on their existing share investments, and further encouraged investment activity.
3. Since 2011, the legislated procedure for streaming franked dividends through a discretionary trust has been embraced in many business and personal investment structures.

The dividend imputation system has heavily influenced domestic investor behaviour for many years now. Policymakers from the major political parties have actively encouraged such investment activity and created an environment which has fostered confidence in many Australians to engage in share investment decision-making.

As we shall see, the removal of refundability will hurt some more than others. In our view, it is important to maintain confidence in the integrity of political decision-making. Any changes proposed to refundability should be preceded by research designed to ascertain whether the taxpayers most adversely impacted are those whose circumstances make them the least capable of altering and adapting their investment strategy.

---

[17] Office of the Chief Economist, *The performance and characteristics of Australian firms with employee share schemes*, Research Paper 4/2017, Luke Hendrickson, Stan Bucifal, Toni Pachernegg, Maria Boyle and David Hansell, July 2017. Source: https://www.industry.gov.au/sites/g/files/net3906/f/June%202018/document/pdf/the_performance_and_characteristics_of_australian_firms_with_employee_share_schemes.pdf

[18] ATO, *Income test for the upfront concession – $1,000 reduction*. Source: https://www.ato.gov.au/general/employee-share-schemes/employees/ess-and-your-tax/income-test-for-the-upfront-concession---$1,000-reduction/

[19] ASX Australian Investor Study 2017. Prepared by Deloitte Access Economics. Source: https://www.asx.com.au/education/2017-asx-investor-study.htm

The Interim Findings of the Hayne Royal Commission

Committee members may wish to reflect on the fact that their inquiry coincides with the final stages of The Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry.

At a time when the conduct of some of our financial institutions (including APRA regulated superannuation funds) has been called into question, the Committee is deliberating on a measure which, if implemented, would discourage many Australians from taking greater control of their financial affairs by directly or indirectly investing in shares yielding franking tax offset entitlements, or establishing a self-managed superannuation fund to do so, and so avoid the high fees and questionable service offerings exposed by Commissioner Hayne at some of our largest financial institutions.

The impact of refundable franking tax offsets on various shareholder types

The impact of refundable franking tax offsets on Australian listed companies

In general terms:

- Australian companies are ineligible for refundable franking tax offsets when calculating their own taxable income. Instead, any unused franking tax offset may be capable of being converted into a tax loss capable of being carried forward to future use[20].
- Companies whose franking accounts are reliably in surplus have responded favourably to shareholder demand for franked dividends (preferably *fully*-franked dividends). Companies regularly communicate general information about their franking capability to shareholders and other stakeholders (e.g. regulators, brokers and financial advisers).
- Companies needing to retain cash for re-investment can offer their shareholders dividend reinvestment plans, seen by many individual shareholders as a “win-win” (i.e. franking tax offset entitlements, plus more shares paid for by the application of the cash dividend forgone acquired for nil brokerage).
- Any share buyback conducted by the company can often be structured to pass on franking tax offset entitlements for that part of the buyback consideration which comprises a dividend.
- Dividend imputation has been a factor in companies deciding whether to offer employee share acquisition schemes, with franking tax offset entitlements flowing to workers directly or via the trust which typically manages the ESS.
- One way to gauge the impact of imputation on the cost of capital for larger, listed companies is through studies of the market value of imputation credits. While these studies report varying estimates, taken together they support the conclusion that imputation has a real but muted impact on the cost of capital for listed companies, and that the availability of foreign equity capital also influences the cost of capital and market valuation of listed Australian companies. That said, residents and Australian funds hold much of the total value of equity on issue by Australian enterprise groups.

The impact of refundable franking tax offsets on Australian private companies

In general terms:

- See above comments about Australian companies being ineligible for refundable franking tax offsets when calculating their own taxable income.
- For an active company carrying on business, franking capability is a sign the company is profitable (i.e. because a surplus in the company’s franking account indicates that tax is being paid on profits derived directly or indirectly). Director shareholders can extract franked dividends on a regular basis, or store franking credits in the company’s franking account for later distribution. Note however that those small to medium sized companies eligible for the

[20] Section 36-55 ITAA 1997.

27.5% company tax rate (declining eventually to 25%) are restricted by the lower company tax rate they enjoy on the extent to which they can attach franking credits to dividends paid to their shareholders.

- The dividend imputation system underpins a popular wealth creation strategy for those able to invest indirectly in listed Australian companies via a passive investment company. The passive investment company derives franked dividends and can "warehouse" the associated franking credits in its own franking account for on-distribution at a time which suits the financial plans of the shareholders of the private company. The passive investment company also generates franking credits in its own right by paying company tax on non-franked dividend income derived (e.g. rent, interest, unfranked dividends)[21].
- For some shareholder \ directors, any latent franking capability in their private company is intended to be utilised in retirement to supplement living costs. The recently introduced caps on superannuation contributions and balances have only added to the popularity of this strategy.

The impact of refundable franking tax offsets on resident individuals

In general terms:

- Dividend imputation – launched at a time which coincided with the privatisation of many iconic Australian government-owned business enterprises – encouraged many Australians to acquire shares directly. Subsequent floats of companies with Australian operations have further attracted retail investor interest. Today, Australia has high levels of *direct* share ownership[22].
- Fund managers and listed investment companies have also long recognised retail investor interest in *indirectly* acquiring shares yielding franked dividends. Guided by financial planners and courted by investment funds, Australians now have many collective investment pathways to access franked dividend streams.
- Despite the complexity of Australia's income tax system, individuals with investments yielding franked dividends typically exhibit a high level of understanding of the impact which the franking tax offset has on their after-tax returns. The offset is readily apparent on the annual ATO notice of assessment and dividend distribution statements also highlight the entitlement.
- Those on lower incomes eligible for a refund of excess franking tax offsets have come to rely on it in a *cashflow* sense. There appears to be no enthusiasm in Australian policy-making circles to compensate the saving efforts of low income earners generally (e.g. by exempting from income tax small amounts of interest derived by low income earners)[23].
- Individuals eligible for a refund can either:
    - Claim via their annual income tax return, or
    - (If they do not need to lodge an annual tax return), lodge online using myGov.com and a special form developed by the ATO[24]. The process is quick and easy thanks to the dividend pre-fill information already in the ATO's possession.
- Australia's resident individual income tax rates – coupled with each person's circumstances and stage of life – are key to any discussion about franking tax offset entitlements. For example, the $18,200 tax free threshold encourages some parents and relatives to acquire shares in the name of children and young adults[25]. In the experience of Chartered Accountants

---

[21] Recent amendments to the tax law enable passive investment companies to pay tax at 30%.
[22] ASX Australian Investor Study 2017, op cit.
[23] In the United Kingdom for example, many individuals can earn some interest from their savings without paying tax. Refer: https://www.gov.uk/apply-tax-free-interest-on-savings.
[24] ATO website, *Refunding excess franking credits – individuals. Apply for a refund*. Source: https://www.ato.gov.au/individuals/investing/in-detail/investing-in-shares/refunding-franking-credits---individuals/?page=3#Apply_for_a_refund The ATO form for claiming a refund without lodging an income tax return is: *Refund of franking credits instructions and application for individuals 2018* (NAT 4105).
[25] ATO website, *Children's share investments*. Source: https://www.ato.gov.au/individuals/investing/in-detail/investing-in-shares/refunding-franking-credits---individuals/?page=3#Apply_for_a_refund

however, the group most cognisant of the benefits of franked dividends are those who are either actively planning for their retirement, or who have retired.

- We note that Treasury has recently published Table 1 below, setting out the amount of franking credit refunds obtained by taxpayers in each of the personal income tax rate bands.

Table 1: Franking credit refunds – Individuals

Taxable Income	Number of individuals	Percentage of individuals	Franking credits refunded ($ million)
Less than $18,200	610,000	54%	500
$18,201 - $37,000	360,000	32%	800
$37,001 - $87,000	120,000	11%	600
$97,001 - $180,000	30,000	2.60%	200
Greater than $180,000	5,000	0.40%	100

Source: Treasury. Published in Australian Financial Review, 16 March 2018

The data in Table 1 should, if possible, be further developed at the Committee's request to provide greater insights into the *profile* of individuals currently eligible for franking tax offset refunds. For example, the Committee would benefit from:

- Knowing the age profile of these individuals;
- The shares they hold[26] and the amount and nature of the dividends received[27];
- Their age pension entitlements (if any), noting any correlation with assets test[28] data held by the Department of Human Services (DHS);
- Insights from DHS on the extent to which Australians on part age pensions (or close to part-pension eligibility) may choose to divest shares yielding franked dividends to qualify for greater pension entitlements; and
- Insights from the Minister for Social Services about the likely impact which the loss of refundability could have on the deeming rules currently applied to calculate the amount of deemed income DHS includes in the income test for age pension purposes.

Note that Senator David Leyonhjelm (Liberal Democratic Party) sought and obtained detailed costings from the Parliamentary Budget Office (PBO) about curtailing franking tax offset refundability in May 2018. The response is attached as Appendix B.

Recommendation

The Committee should seek to ascertain the extent to which refund denial may cause some individuals to apply for the age pension (or other transfer payment entitlement) or obtain higher pension payments. In this regard, officials from the PBO could be asked to further explain their Key Assumptions and conclusions.

[26] The ATO has access to share transaction data. Source: https://www.ato.gov.au/General/Gen/Share-transactions---20-September-1985-to-30-June-2018-data-matching-program-protocol/
[27] The ATO has access to dividend data. Source: https://www.ato.gov.au/individuals/lodging-your-tax-return/in-detail/pre-fill-availability/?page=7
[28] Refer https://www.humanservices.gov.au/individuals/enablers/assets-test-age-pension/39891

Examples of individual taxpayer outcomes

The Committee will no doubt receive many examples of the impact which curtailing the refund will have on Australians.

On refundable franking credits for example, comparisons like that in Example 1 will occur:

Example 1 – Taxpayer whose only income comprises a fully franked dividend

Karen's only income is from a parcel of shares in ASX listed companies. Using the assumptions in Note 1, her tax calculation under current law and the no-refund model is as follows:

	Current law $	**No refund $**
Assessable income		
Fully franked dividend	50,000	50,000
Gross-up for company tax paid[2]	21,429	21,429
Deductions	0	0
Taxable Income	71,429	71,429
Income tax[3]	14,761	14,761
Medicare levy	1,429	1,429
Franking tax offset	-21,429	-16,190[4]
Tax refund	-5,239	0
Unused franking tax offset	0	5,239
Karen's cash in hand	55,239	50,000

Notes:

1. Assumes a consistent dividend amount franked to the same extent by reference to the 30% company tax rate, received by a taxpayer on the same personal tax scale paying a 2% Medicare levy.
2. Deemed amount included in assessable income.
3. 2017-18 resident individual rates.
4. Entitlement ($21,429) limited to amount which reduces Karen's tax to nil ($16,190).

Example 2 – Taxpayer receiving dividend and non-dividend income

Kevin's assessable income comprises both bank interest and franked dividends.

Assessable income	
Interest	15,000
Fully franked dividend	20,000
Gross-up	8,571
Deductions	0
Taxable Income	43,571
Tax	5,708
Medicare levy	871
Franking tax offset	-8,571
Cash refund	-1,992

As indicated, imputation is a mechanism to ensure Kevin's income is taxed at his actual individual marginal rate. Any loss of the refund will prompt Kevin (if he can) to seek to increase non-franked dividend income to utilise the excess franking tax offset.

A "pensioner guarantee" but only for the lucky few?

- Shortly after making its original announcement on franking tax offset refundability, the ALP announced a "Pensioner Guarantee"[29]:

  > "The Pensioner Guarantee means pensioners and allowance recipients will be protected from the abolition of cash refunds for excess dividend imputation credits when the policy commences in July 2019.
  >
  > Self-managed superannuation funds with at least one pensioner or allowance recipient before 28 March 2018 will also be exempt from the changes.
  >
  > This means that every pensioner will still be able to benefit from cash refunds."

- Our sense is that ALP policy advisers had quickly identified *some* of the stakeholder groups adversely impacted by the original announcement. But there are others. For example, why are those who have received large compensation payments because of severe injuries or unable to work because of medical incapacity and receiving superannuation pensions ineligible for refunds?

- Chartered Accountants ANZ feel that Labor's "point in time" eligibility criteria has resulted in a windfall for those (and their superannuation funds) who qualify but fails to recognise those who will *become* pensioners after that date and whose financial circumstances make them just as financially reliant on refundability as those lucky to have been around for the 28 March 2018 cut-off date. As we have already observed, many low-income Australians have literally been banking on continued refundability in their retirement planning.

[29] Shadow Treasurer Chris Bowen, *Labor's plan to crack down on tax loopholes, protect pensioners, and pay for schools and hospitals*, Media release, 27 March 2018. Source: https://www.chrisbowen.net/media-releases/labor-s-plan-to-crack-down-on-tax-loopholes-protect-pensioners-and-pay-for-schools-and-hospitals/

- The Committee would by now be aware of other proposals to cap refundability. The most common proposal appears to be a dollar cap on refundability, calculated by reference to low income, pensioner status etc. Another suggestion is to taper (reduce) refund eligibility as taxable income increases. Both will trigger behavioural or clientele effects as taxpayers position themselves to remain eligible for at least some refund. The Committee should also note that the 45 day holding period rules already contain references to "small" shareholdings, set at a franking tax offset entitlement of $5,000 or less (roughly equivalent to receiving a fully franked dividend from a listed company of $9,000).

Recommendation

The Committee should explore how concepts such as the pensioner guarantee could be further developed to provide on-going refund eligibility for that group of taxpayers who meet eligibility criteria.

Practical problems in implementing a "pensioner guarantee"

- We also see issues emerging for tracking pensioner guarantee eligibility and advising those who will continue to receive refunds. Presumably the Department of Human Services will need to track a pensioner's status and report this to the ATO via data sharing arrangements (this probably happens already). SMSF administrators will need to store this data and put it on one or more SMSF annual returns. Tax distribution statements will need to be re-designed to alert eligible taxpayers of their refund entitlement.
- Also, what happens if an SMSF has members who satisfy the pensioner guarantee rule (e.g. because the fund had an age pension or allowance recipient before 28 March 2018) but those members are no longer in the fund because they voluntarily left or died? Are such funds forever exempt?
- A further example. Assume an SMSF member retired three years ago with money in her SMSF account, was an aged pensioner at that time, but subsequently lost her pensioner status because of the income and / or assets test (e.g. because of a bequest under a relative's will) but became eligible again after 27 March 2018. Presumably because they had been a recipient *before* 28 March then franking credits refunds will be fully available?
- What about an aged pensioner who retired before 28 March 2018 and subsequently elected to move money from an APRA fund to an SMSF? They would move from an entity that can generally utilise all its franking tax offset capability to one that cannot unless some form of "pensioner status tracking" mechanism is introduced.

The impact of refundable franking tax offsets on tax exempt bodies[30]

There are many types of tax exempt organisations in Australia, and this group includes bodies which are *not* charities[31].

In general terms:

- As noted earlier, the lack of refundability in the *original* design of dividend imputation created an incentive to ensure that franking credits were only paid to shareholders who could use the tax offset. Anti-avoidance rules were enacted to (for example) prevent the streaming of franked dividends *away from* to tax-exempt bodies and others such as non-residents taxpayers unable to fully use the franking offset.

---

[30] Refer to the ATO's online publication, *Income tax exempt organisations*. Source: https://www.ato.gov.au/Non-profit/your-organisation/do-you-have-to-pay-income-tax-/income-tax-exempt-organisations/
[31] Refer to the ATO's online publication, *Types of income tax exempt organisations*. Source: https://www.ato.gov.au/Non-profit/your-organisation/do-you-have-to-pay-income-tax-/types-of-income-tax-exempt-organisations/

- The introduction of refundability in 2000 turned this thinking around insofar as tax exempt bodies were concerned, making franked dividends an extremely attractive investment for such organisations.
- Nowadays, the refundable franking tax offset provides obvious substantial cash benefits to those tax-exempt bodies with the means and the mandate to invest in Australian resident companies which pay franked dividends. The ATO and Australian Charities and Not-for-profits Commission can no doubt assist the Committee with relevant data on the value refundability provides to the sector.
- We note that the ALP's stated policy to curtail refundability does not apply to "charities and not-for-profit institutions, such as universities"[32]. The Shadow Treasurer, Chris Bowen, has also been quoted as saying that Australia's $149 billion Future Fund will remain eligible for refunds[33].

Recommendation

The Committee should identify the range of organisations which, under Labor's proposed model, would continue to receive refunds of excess franking tax offsets and consider the policy rationale.

The value of the associated tax expenditure should be quantified.

The Committee may also wish to explore whether *all* tax-exempt organisations should be eligible for refunds. The point we are making here is that not all tax-exempt organisations are formed for *charitable* purposes. Some exist to benefit specific groups within society or support specific goals.

The impact of refundable franking tax offsets to APRA regulated superannuation funds

In general terms:

- The size of APRA regulated funds and the diversified nature of the investment mandates they usually employ mean that the franking tax offset is more likely to be fully utilised because of the income tax payable on non-franked dividend income, rather than create a refund entitlement.
- That said, a significant minority of APRA regulated super funds are recipients of refunds because of their member profile (e.g. a substantial number of members in pension phase). APRA and the relevant industry association can provide more details.
- There has often been interest in *how* large funds allocate franking tax offsets to member accounts, particularly those in pension phase.
- There have already been media reports that large funds will commercially benefit from the curtailment of refundability and the impact this may have on SMSFs[34]. It is said that some SMSF trustees will explore rolling over their arrangements to a larger fund, thus minimising the risk of "wasted" excess franking tax offsets and obtaining other benefits (e.g. asset diversification, professional fund investment and management services, greater protection from the administration problems sometimes encountered as SMSF trustees age and encounter illness).

The impact of refundable franking tax offsets to self-managed superannuation funds (SMSFs)

---

[32] Shadow Treasurer Chris Bowen, *A fairer tax system: Dividend imputation reform*, Media release, 13 March 2018. Source: https://www.chrisbowen.net/media-releases/a-fairer-tax-system-dividend-imputation-reform/

[33] Jacob Greber, *Future Fund billions exempted from Labor dividend crackdown*, The Australian Financial Review, 15 March 2018. Source: https://www.afr.com/news/economy/future-fund-billions-exempted-from-labor-dividend-crackdown-20180315-h0xihx

[34] Joanna Mather, *Pooled super funds will do better under Labor's changes*, The Australian Financial Review, 14 March 2018. Source: https://www.afr.com/news/policy/tax/pooled-super-funds-will-do-better-under-labors-changes-20180314-h0xfzr

In general terms:

- The 15% income tax rate enjoyed by complying SMSFs make fully franked dividends from Australian companies (typically franked by reference to the 30% "large" company tax rate) obviously attractive.
- Small to medium-sized SMSFs would be substantially impacted by the denial of refunds. Dividend imputation has been an important contributing factor to the growth in the number of SMSFs, firstly because of the tax shelter provided and then (from 2000) the full refund. It is anticipated that larger SMSFs would more readily adapt to refund curtailment by including greater diversity in their investment strategy to generate more non-franked dividend income streams.
- Although we lack up to date data, we expect the Committee will conclude that the asset allocation of SMSFs is often weighted towards Australian listed company shares yielding franked dividends.
- SMSF trustees (typically spouses) usually demonstrate a clear understanding of the way in which the franking tax offset boosts investment returns compared to alternative investments (e.g. shares in overseas domiciled companies).
- Some commentators have expressed concern that SMSFs often lack a diversified investment strategy. Indeed, the Shadow Treasurer Chris Bowen is reported to have said that Labor's plan to curtail refundability would help de-risk the retirement savings pool[35]. Whilst diversification is indeed sound advice, the Committee should note that SMSF trustees also tend to favour Australian listed company shares for many other reasons, including:
    - their familiarity with the brands and businesses conducted
    - the comparative ease of buying and selling shares locally
    - the ready availability of local media commentary, research and data about their investments
    - accounting systems linked to broker or financial planner reporting platforms
    - confidence in the domestic regulatory environment
    - ability to attend Annual General Meetings in person, vote and ask questions
    - no foreign exchange risk
    - not having to deal with foreign tax regimes or administrators, and
    - the perception that the Australian economy is strong and less prone to volatility.

Possible secondary effects of curtailing refundability

As noted earlier, refundability has influenced taxpayer behaviour. Any move to curtail refundability is likely to have a range of secondary effects, including:

(a) The start date rush

Labor's original announcement was that refunds would be curtailed from 1 July 2019. With a Federal Election to be held by 18 May 2019, a Labor victory at the polls could see a frenzy of activity in the lead-up to 1 July 2019 without taxpayers necessarily having the benefit of enacted legislation to guide them.

Any rush to adjust portfolios may lead to some short-term volatility on the ASX although the

[35] Andrew Tillett, *New modelling says Labor franking credits plan would hit super funds up to 9pc*, The Australian Financial Review, 25 September 2018. Source: https://www.afr.com/news/new-modelling-says-labor-franking-credits-plan-would-hit-super-funds-up-to-9pc-20180924-h15sia

Committee should seek expert opinion on the likelihood that this might occur.

Some listed companies may seek to assist shareholders by providing a facility for small parcels to be sold free of brokerage.

We also predict increased off-market listed share transfers between SMSFs and associates.

Chartered Accountants ANZ supports sensible implementation timeframes with clear guidance, particularly for measures which impact genuine, long-term investment and retirement planning. For example, refundability could be phased out rather than introduced with immediate effect.

(b) At the Australian company level

- We think it likely that there will be increased demands on Australian companies to declare fully franked dividends in the lead-up to the date from which refundability is curtailed.
- As noted earlier however, there are a range of anti-streaming rules and the ATO is likely to be called upon to opine on whether these anti-avoidance rules apply to any once-off arrangements (such as off-market share buy-backs) to distribute franking tax offset entitlements. For example, the ATO has a Taxpayer Alert relevant to when a company with a significant franking credit balance raises new capital from existing or new shareholders[36].
- The Committee should also note that debt financing the payment of dividends generally attracts interest deductions for the borrowing corporate taxpayer under the so-called *Roberts & Smith* principle[37].
- Some Australian companies which currently offer (frankable) preference share arrangements may choose not to do so in future. For some shareholder profiles, such instruments are seen as a reliable source of franking credits, and issuers have taken this into account in setting the rate of return.
- There could also be an increase in the range or type of shareholder distributions on offer from Australia's listed companies. Some Australian companies may consider offering debt (unfrankable) instruments to resident shareholders and other investors for example.
- For companies with cross-border operations, we expect greater management focus on whether it is preferable for the company to pay *Australian* income tax (which generate franking credits in the company's franking account), as distinct from foreign income tax payments from the conduct of business overseas which, in many cases, can be repatriated to Australia as non-assessable non-exempt income in the hands of the Australian company. If this occurs, we may see more *partially*-franked dividends rather than fully-franked dividends.

(c) At the superannuation fund level

- Some SMSF trustees may decide to roll to an APRA regulated fund where full franking tax offset utilization is possible. Rumours circulating within the industry suggest that some APRA regulated funds will actively court SMSF rollovers. We do not believe it is good policy to be effectively favouring, by implication, different types of superannuation entities.
- Funds which currently generate franking tax offset refunds may explore ways to generate non-franked dividend income.
- Apart from investing in non-franked dividend income streams, funds may also explore the more

[36] Taxpayer Alert 2015/2. Source: http://law.ato.gov.au/atolaw/view.htm?docid=%22TPA%2FTA20152%2FNAT%2FATO%2F00001%22
[37] Tax Ruling 95/25. Source: http://law.ato.gov.au/atolaw/view.htm?rank=find&criteria=AND~roberts~basic~exact&sis=smith&target=EA&style=java&sdocid=TXR/TR9525/NAT/ATO/00001&recStart=1&PiT=99991231235958&Archived=false&recnum=11&tot=23&pn=RDB:::RDB

effective use of the 33.3% CGT discount available to complying funds. We note the Australian Labor Party's proposal to halve (from 50% to 25%) on a prospective basis the CGT discount for resident individuals on assets held directly or via flow-through partnership and trusts[38]. We are unaware of any Labor proposal to reduce the 33.3% discount currently available to complying superannuation funds.

- For APRA funds, we suggest the Committee seek expert witnesses who can comment on what curtailment of refunds might mean vis-à-vis the ability of Australian funds to match the investment power of foreign funds which frequently express interest in key Australian assets such as infrastructure.

(d) At the individual resident investor level

- Although much depends on the profile of each company of course, well-advised Australian investors are typically attracted to *both* the franked dividend yield and the growth prospects of Australian listed companies. Shares are also quite accessible to investors. Small parcels can be acquired initially and a portfolio gradually built over time.
    - To the extent curtailing refundability results in diverting investor interest to debt instruments or other types of low growth investments, the Committee may want to consider the ramifications in terms of risk, investor education and the possibility that a lower growth investment strategy may result in an investor becoming reliant on the age pension at an earlier age.
    - Similarly, to the extent some investors shift to more speculative investments the Committee may wish to consider the broader economic impact of investors having increased exposure to volatility. For example, high-yield unlisted property trusts can be a trap for some.

[38] ALP policy document, *Positive plan to help housing affordability*, ALP website. Source: https://www.alp.org.au/negativegearing

Appendix B

PBO response to Senator David Leyonhjelm

Policy costing

Dividend imputation credit refunds	
Person/party requesting the costing:	Senator David Leyonhjelm, Liberal Democratic Party
Date costing completed:	4 May 2018
Expiry date of the costing:	The release of the 2018-19 Budget.
Status at time of request:	Submitted outside the caretaker period ☒ Confidential ☐ Not confidential
Summary of proposal: The proposal involves two options to change the tax treatment of franking credits attached to distributions (otherwise known as imputation credits) from a refundable tax offset to a non-refundable tax offset: • Option 1: Make franking credits non-refundable for all individuals and superannuation funds. • Option 2: Make franking credits non-refundable for individuals and superannuation funds, except for recipients of Australian Government pensions and allowances with individual shareholdings, and self-managed superannuation funds with at least one member who is an Australian Government pension or allowance recipient before 28 March 2018. The proposal would have effect from 1 July 2019. The request sought details on the following as a proportion of gross domestic product (GDP) from 2004-05 to 2014-15: • superannuation earnings tax before franking credits • franking credits associated with this earnings tax • earnings tax after franking credits • company tax paid giving rise to those franking credits. The request also specified tables for the number of individuals and superannuation funds directly affected in 2019-20 and specified tables for the analysis of individuals and superannuation funds in 2014-15.	

Costing overview

Background

Dividend imputation applies to some Australian-source dividend income, reducing the amount of income tax paid by Australian resident shareholders.

Under the dividend imputation system, Australian resident companies that distribute dividends from after-tax profits have the option of passing on franking credits (also known as imputation credits) to their shareholders, attached to the dividends they receive. This provides shareholders with a credit for the tax that a company has paid on its profits.

Shareholders include an amount equal to the franking credit attached to their dividend in their assessable income for tax purposes. Australian residents and complying superannuation funds are entitled to claim a tax offset equal to the amount of franking credits included in their income.

This franking credit tax offset can be used to reduce a taxpayer's tax liability from all forms of income. Currently, any excess franking credits are refunded to the taxpayer by the Australian Taxation Office (ATO).

Under Option 1, franking credits would become non-refundable for all individuals and superannuation funds. Under Option 2, franking credits would become non-refundable for individuals who do not receive an Australian Government pension or allowance and for superannuation funds, except for self-managed superannuation funds with at least one member who is an Australian Government pension or allowance recipient before 28 March 2018.

Financial impact

Option 1 would be expected to increase the fiscal and underlying cash balances by $5,597 million over the 2017-18 Budget forward estimates period. This impact primarily reflects increases in revenue, but also includes a non-ongoing increase in departmental expenses for the ATO.

Table 1: Financial implications ($m) – Option 1 (no exclusions)[(a)(b)]

	2017–18	2018–19	2019–20	2020–21	**Total to 2020–21**
Fiscal balance	-	-2	-1	5,600	**5,597**
Underlying cash balance	-	-2	-1	5,600	**5,597**

(a) A positive number represents an increase in the relevant budget balance; a negative number represents a decrease.

(b) Figures may not sum to totals due to rounding.

\- Indicates nil.

Option 2 would be expected to increase the fiscal and underlying cash balances by $5,197 million over the 2017-18 Budget forward estimates period. This impact primarily reflects increases in revenue, but also includes a non-ongoing increase in departmental expenses for the ATO.

Table 2: Financial implications ($m) – Option 2 (excluding Australian Government pension and allowance recipients)[(a)(b)(c)]

	2017–18	2018–19	2019–20	2020–21	**Total to 2020–21**
Fiscal balance	-	-2	-1	5,200	**5,197**
Underlying cash balance	-	-2	-1	5,200	**5,197**

(a) A positive number represents an increase in the relevant budget balance; a negative number represents a decrease.
(b) Figures may not sum to totals due to rounding.
(c) The proposal would not apply to individuals who receive Australian Government pension and allowance payments in the year of assessment. The proposal would also not apply to self-managed superannuation funds with at least one member who is a recipient of an Australian Government pension or allowance payment before 28 March 2018.
\- Indicates nil.

Both options would be expected to have an ongoing financial impact beyond the 2017-18 Budget forward estimates period. The detailed financial implications of both options over the period to 2027-28 are included at Attachment A.

Both options of the proposal would be expected to result in an increase in departmental expenses of $2 million in 2018-19 and $1 million in 2019-20. These expenses reflect the cost to the ATO of implementing the proposal, including compliance, system changes and information campaigns.

This costing is subject to uncertainties surrounding income and population growth rates, changes in the number of individuals and superannuation funds with excess franking credits, changes to dividend payout ratios, relative returns between asset classes, preferences of self-managed superannuation fund account holders, volatility in the earnings of companies that pay franked distributions, and behavioural responses to recent superannuation measures. There are also significant uncertainties around the behavioural responses of affected individuals, superannuation funds and companies to the proposal.[39]

The requested details on superannuation earnings tax, superannuation franking credits, superannuation earnings tax after franking credits and company tax paid giving rise to those franking credits is provided at Attachment B. The value of franking credits is equal to the company tax paid giving rise to those franking credits, as a franking credit balance only arises where company tax is paid. The timing of the payment of company tax associated with the claimed franking credits is not separately identifiable.

The specified distributional analysis of the number of individuals and superannuation funds directly affected in 2019-20 and analysis of individuals and superannuation funds in 2014-15 are included at Attachment C.

Key assumptions

- There are a number of potential behavioural responses to the proposal from individuals and superannuation funds, as well as from companies that distribute franked dividends.
  - For individuals, potential behavioural responses could include shifting from shares to alternative investment arrangements (including to investments within superannuation), and couples shifting the ownership of shares from the lower income earner to the higher income earner such that the higher income earner can utilise the franking credits as a non-refundable tax offset.
  - For superannuation funds, potential behavioural responses could include rolling assets from a fund with negative net tax to a fund with positive net tax, changing funds' asset portfolio allocations, or changing the membership structure of the fund, in order to maximise the utilisation of franking credits.
  - For companies, a potential behavioural response could include changing the amount of dividends distributed (and profits withheld) or the level of dividend franking due to the decrease in the value of franking credits for some shareholders.

- Behavioural responses to the changes to the treatment of franking credits have been incorporated into this costing for individuals and superannuation funds with excess franking credits. This has led to a reduction in the revenue gain arising from the proposal.

- Under Option 2, the PBO has assumed that the number of superannuation funds with a member who was a recipient of an Australian Government pension or allowance before 28 March 2018 would decline over time.

- The impact on payments to Australian Government pension and other income support recipients due to changing the tax treatment of franking credits would not be expected to be significant over the time period examined and has not been included in this costing.

[39] There are inherent uncertainties in all policy costings, regardless of who produces them. For a more detailed discussion of the nature and sources of these uncertainties see PBO information paper no. 01/2017, *Factors influencing the reliability of policy proposal costings.*

- Over the longer term, the proposal may lead to changes in assets held directly by, or through the superannuation accounts of individuals which may subsequently result in a change in means-tested payments. The PBO does not expect this impact to be significant over the time period examined.

Methodology

Costing

- The costing was based on a 16 per cent sample of de-identified personal income tax returns for the 2014-15 financial year, tax schedules for superannuation funds (including self-managed superannuation funds) for the 2013-14 and 2014-15 financial years, and the full dataset of de-identified personal income tax returns for the 2013-14 financial year.
- The data was used to estimate the amount of revenue expected to be collected under current policy settings (including the recent superannuation policy changes and scheduled company and individual tax rate changes), and then again if franking credits were changed from a refundable tax offset to a non-refundable tax offset for affected individuals and superannuation funds, as outlined in this proposal. An adjustment was made for individuals and superannuation funds with excess franking credits to account for behavioural responses to the proposal.
  - The costing was derived by calculating the difference in revenue under these two scenarios.
- The modelling has taken into account the timing of tax collections.
- Departmental expenses were estimated based on amounts allocated to the ATO for measures with similar administrative complexity.
- Revenue estimates have been rounded to the nearest $100 million. Departmental expense estimates have been rounded to the nearest $1 million.

Historical budget analysis at Attachment B

The PBO has made assumptions relating to the conversion of revenue (an accrual measure) to receipts (a cash measure) for contributions tax, earnings tax and franking credits.

The total amount of assessable superannuation contributions was calculated by deducting insurance premiums and superannuation surcharges from total assessable contributions. The 15 per cent statutory tax rate was applied to this amount to derive total contributions tax. A timing assumption was applied to convert from accrual to cash estimates. Earnings tax was then estimated as the residual of total superannuation taxes after excluding contribution tax.

The accrual measure of franking credits was converted to a cash measure using a timing assumption. The timing reflects that franking credits are only claimed on assessment, and has the effect of shifting the cash basis of franking credits from one financial year to the next.

Data sources

- The ATO provided a 16 per cent sample of de-identified personal income tax returns for the 2014-15 financial year, tax schedules for superannuation funds (including self-managed superannuation funds) for the 2013-14 and 2014-15 financial years, and the full dataset of de-identified personal income tax returns for the 2013-14 financial year.
- ATO, 2017, *Superannuation fund data to 2014-15*, Canberra: Commonwealth of Australia.
- ATO, 2017, *Taxation Statistics 2014-15*, Canberra: Commonwealth of Australia.
- Treasury provided economic forecasts for personal income and superannuation tax as at the 2017-18 Mid-year Economic and Fiscal Outlook report.
- PBO, 2014, 01/2014 *Trends in Australian Government Receipts 1982-83 to 2012-13*, Canberra: Commonwealth of Australia.

- RiceWarner, 2017, *Superannuation Market Projections*, Sydney: RiceWarner.

Attachment A – Dividend imputation credit refunds – financial implications

Table A1: Dividend imputation credit refunds – Option 1 (no exclusions) – Fiscal and underlying cash balances ($m)[(a)(b)]

	2017–18	2018–19	2019–20	2020–21	2021–22	2022–23	2023–24	2024–25	2025–26	2026–27	2027–28	Total to 2020–21	Total to 2027–28
Revenue													
Superannuation funds	-	..	..	*3,400*	*3,600*	*4,000*	*4,400*	*4,500*	*4,900*	*5,000*	*5,100*	***3,400***	***34,900***
Individuals	-	..	..	*2,200*	*2,200*	*2,200*	*2,300*	*2,100*	*2,000*	*1,900*	*1,800*	***2,200***	***16,700***
Total - revenue	**-**	**..**	**..**	**5,600**	**5,800**	**6,200**	**6,700**	**6,600**	**6,900**	**6,900**	**6,900**	**5,600**	**51,600**
Expenses													
Departmental													
Australian Taxation Office	-	*-2*	*-1*	-	-	-	-	-	-	-	-	***-3***	***-3***
Total - expenses	**-**	**-2**	**-1**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-3**	**-3**
Total	**-**	**-2**	**-1**	**5,600**	**5,800**	**6,200**	**6,700**	**6,600**	**6,900**	**6,900**	**6,900**	**5,597**	**51,597**

(a) A positive number for the fiscal balance indicates an increase in revenue or a decrease in expenses or net capital investment in accrual terms. A negative number for the fiscal balance indicates a decrease in revenue or an increase in expenses or net capital investment in accrual terms. A positive number for the underlying cash balance indicates an increase in receipts or a decrease in payments or net capital investment in cash terms. A negative number for the underlying cash balance indicates a decrease in receipts or an increase in payments or net capital investment in cash terms.

(b) Figures may not sum to totals due to rounding.

.. Not zero but rounded to zero.

\- Indicates nil.

Table A2: Dividend imputation credit refunds – Option 2 (excluding Australian Government pension and allowance recipients) – Fiscal and underlying cash balances ($m)[(a)(b)(c)]

	2017–18	2018–19	2019–20	2020–21	2021–22	2022–23	2023–24	2024–25	2025–26	2026–27	2027–28	Total to 2020–21	Total to 2027–28
Revenue													
Superannuation funds	-	..	..	*3,300*	*3,600*	*3,900*	*4,300*	*4,400*	*4,800*	*5,000*	*5,100*	***3,300***	***34,400***
Individuals	-	..	..	*1,900*	*1,900*	*1,900*	*1,900*	*1,800*	*1,700*	*1,600*	*1,500*	***1,900***	***14,200***
Total - revenue	**-**	**..**	**..**	**5,200**	**5,500**	**5,800**	**6,200**	**6,200**	**6,500**	**6,600**	**6,600**	**5,200**	**48,600**
Expenses													
Departmental													
Australian Taxation Office	-	*-2*	*-1*	-	-	-	-	-	-	-	-	***-3***	***-3***
Total - expenses	**-**	**-2**	**-1**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-3**	**-3**
Total	**-**	**-2**	**-1**	**5,200**	**5,500**	**5,800**	**6,200**	**6,200**	**6,500**	**6,600**	**6,600**	**5,197**	**48,597**

(a) A positive number for the fiscal balance indicates an increase in revenue or a decrease in expenses or net capital investment in accrual terms. A negative number for the fiscal balance indicates a decrease in revenue or an increase in expenses or net capital investment in accrual terms. A positive number for the underlying cash balance indicates an increase in receipts or a decrease in payments or net capital investment in cash terms. A negative number for the underlying cash balance indicates a decrease in receipts or an increase in payments or net capital investment in cash terms.

(b) Figures may not sum to totals due to rounding.

(c) The proposal would not apply to individuals who receive Australian Government pension and allowance payments in the year of assessment. The proposal would also not apply to self-managed superannuation funds with at least one member who is a recipient of an Australian Government pension or allowance payment before 28 March 2018.

.. Not zero but rounded to zero.

\- Indicates nil.

Attachment B – Superannuation earnings tax and franking credits as a proportion of GDP

Contributions tax and earnings tax are not separately identifiable in tax collections. As such, the split between the two was estimated and is subject to uncertainties arising from assumptions required to separately identify earnings tax and contributions tax.

Table B1: Superannuation earnings tax before and after franking credits as a proportion of GDP – 2004-05 to 2014-15

Per cent of GDP	2004–05	2005–06	2006–07	2007–08	2008–09	2009–10	2010–11	2011–12	2012–13	2013–14	2014–15
Earnings tax before franking credits	0.44	0.46	0.49	0.77	0.42	0.21	0.19	0.37	0.28	0.19	0.20
Franking credits[(a)]	0.25	0.35	0.39	0.44	0.37	0.36	0.30	0.49	0.38	0.38	0.44
Earnings tax[(b)]	**0.19**	**0.11**	**0.11**	**0.33**	**0.05**	**-0.15**	**-0.11**	**-0.12**	**-0.10**	**-0.19**	**-0.24**

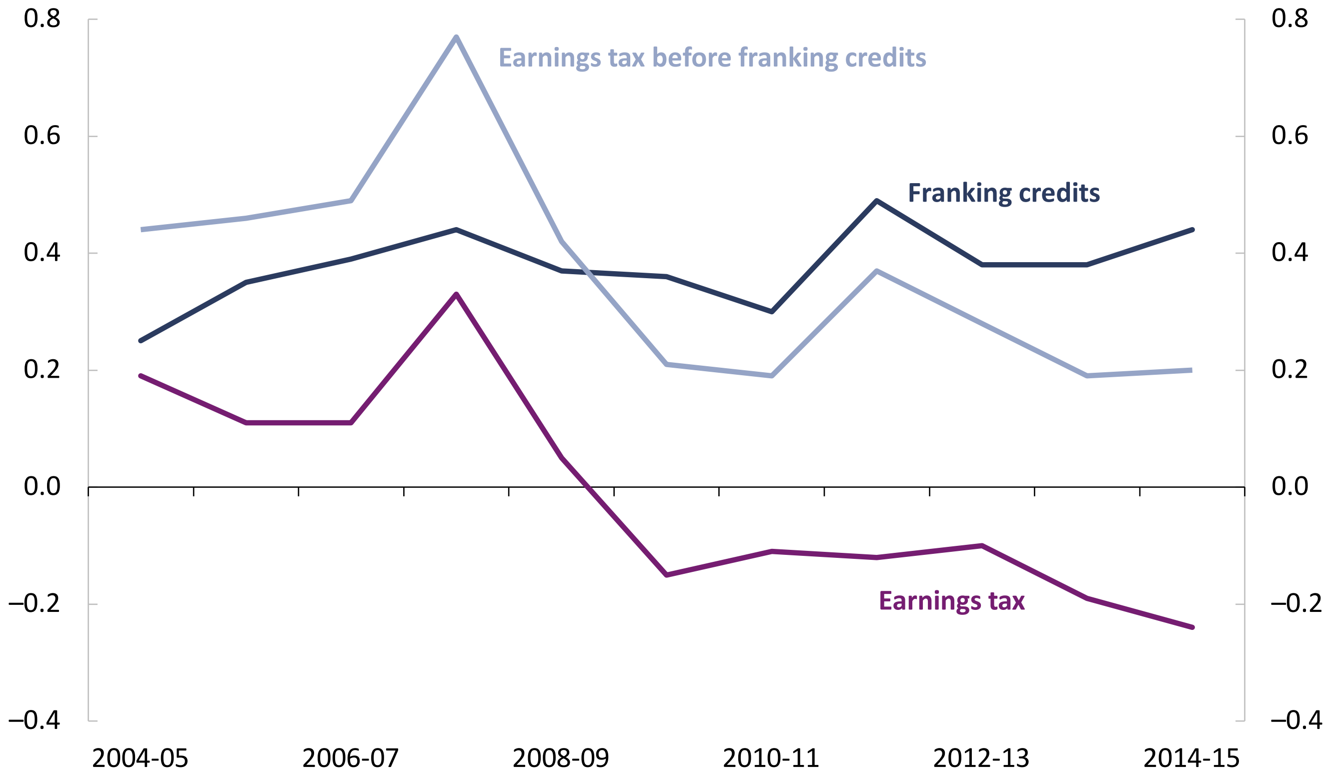
(a) The value of franking credits is equal to the company tax paid giving rise to those franking credits, as a franking credit balance only arises where company tax is paid. The timing of the payment of company tax associated with the claimed franking credits is not separately identifiable.

(b) Earnings tax before franking credits plus franking credits.

Chart B1: The effect of franking credits on superannuation earnings tax

Per cent of GDP

Per cent of GDP


0.8
0.6
0.4
0.2
0.0
−0.2
−0.4
Earnings tax before franking credits
Franking credits
Earnings tax
2004-05
2006-07
2008-09
2010-11
2012-13
2014-15

Attachment C – Dividend imputation credit refunds – distributional analysis

Table C1: Option 1 — Individual taxpayers directly affected in 2019-20, by pension status

Pension status	Number of taxpayers directly affected
Australian Government pension and allowance recipients	*320,000*
Not an Australian Government pension and allowance recipient	*840,000*
Total individual taxpayers	**1,160,000**

Table C2: Option 1 — Superannuation funds directly affected in 2019-20

<table>
<tr><th colspan="2">Superannuation fund status</th><th>Number of funds directly affected</th></tr>
<tr><td rowspan="2">Self-managed superannuation funds</td><td>Contains a member receiving an Australian Government pension and allowance[a]</td><td>20,000</td></tr>
<tr><td>Does not contain a member receiving an Australian Government pension and allowance[a]</td><td>210,000</td></tr>
<tr><td colspan="2">Total self-managed superannuation funds</td><td>230,000</td></tr>
<tr><td colspan="2">APRA-regulated superannuation funds</td><td>2,300</td></tr>
<tr><td colspan="2">Total superannuation funds</td><td>232,300</td></tr>
</table>

(a) As at 28 March 2018.

Table C3: Option 2 — Individual taxpayers directly affected in 2019-20, by pension status

Pension status	Number of taxpayers directly affected
Australian Government pension and allowance recipients	-
Not an Australian Government pension and allowance recipient	*840,000*
Total individual taxpayers	**840,000**

\- Indicates nil.

Table C4: Option 2 — Superannuation funds directly affected in 2019-20

<table>
<tr><th colspan="2">Superannuation fund status</th><th>Number of funds directly affected</th></tr>
<tr><td rowspan="2">Self-managed superannuation funds</td><td>Contains a member receiving an Australian Government pension and allowance[a]</td><td>-</td></tr>
<tr><td>Does not contain a member receiving an Australian Government pension and allowance[a]</td><td>210,000</td></tr>
<tr><td colspan="2">Total self-managed superannuation funds</td><td>210,000</td></tr>
<tr><td colspan="2">APRA-regulated superannuation funds</td><td>2,300</td></tr>
<tr><td colspan="2">Total superannuation funds</td><td>212,300</td></tr>
</table>

(a) As at 28 March 2018.
- Indicates nil.

Table C5: Individuals — Distribution by taxable income in 2014-15[a]

Decile[b]	Taxable income range	Number of individuals claiming excess franking credits	Percentage claiming excess franking credits	Average excess franking credits claimed ($)[c]	Total excess franking credits claimed ($m)[d]
1	Under $9,500	403,700	29.5%	640	258.8
2	$9,500 to $19,000	267,700	19.3%	990	266.3
3	$19,000 to $26,400	198,700	14.3%	1,580	312.9
4	$26,400 to $35,000	112,900	8.1%	2,980	336.6
5	$35,000 to $43,200	53,200	3.8%	4,430	236.1
6	$43,200 to $52,500	24,200	1.7%	4,670	112.8
7	$52,500 to $64,400	17,000	1.2%	5,040	85.7
8	$64,400 to $80,200	22,500	1.6%	6,030	136.0
9	$80,200 to $109,600	16,100	1.2%	5,980	96.0
10	$109,600 and over	16,300	1.2%	11,880	193.8

Total individual taxpayers	**1,132,300**	**8.1%**	**1,800**	**2,035.1**

(a) Figures may not sum to totals due to rounding.
(b) Based on the income of all taxpayers in 2014-15.
(c) Calculated as the average franking credit refund of those individuals who received a refund in 2014-15.
(d) Calculated as *the number claiming excess franking credits* multiplied by the *average excess franking credits claimed*.

Table C6: Self-managed superannuation funds (SMSFs) — Distribution by fund balance in 2014-15[(a)]

Decile [(b)]	Fund balance range	Number of funds claiming excess franking credits	Percentage claiming excess franking credits	Average excess franking credits claimed ($)[(c)]	Total excess franking credits claimed ($m)[(d)]
1	$0 to $90,276	8,616	17.9%	1,391	12.0
2	$90,277 to $181,089	9,503	19.8%	1,137	10.8
3	$181,090 to $279,252	11,866	24.7%	1,900	22.5
4	$279,253 to $402,090	15,349	31.9%	2,890	44.4
5	$402,091 to $558,140	18,554	38.6%	4,088	75.8
6	$558,141 to $762,242	21,902	45.5%	5,611	122.9
7	$762,243 to $1,044,621	24,734	51.4%	7,532	186.3
8	$1,044,622 to $1,497,218	27,208	56.5%	10,468	284.8
9	$1,497,219 to $2,443,843	29,946	62.2%	15,652	468.7
10	$2,443,843 and over	33,761	70.2%	40,468	1,366.2
Total SMSFs		**201,439**	**41.9%**	**12,880**	**2,594.5**

(a) Figures may not sum to totals due to rounding.
(b) Based on the fund balance of all self-managed superannuation funds in 2014-15.
(c) Calculated as the average franking credit refund of those funds who received a refund in 2014-15.
(d) Calculated as *the number claiming excess franking credits* multiplied by the *average excess franking credits claimed*.

Table C7: Self-managed superannuation funds (SMSFs) with large balances or high excess franking credit amounts in 2014-15

Average excess franking credits claimed by the top percentile of fund balances	$83,000[(a)]
Number of funds claiming more than $2.5 million in excess franking credits	Less than 5[(b)]

(a) Rounded to the nearest $1,000.
(b) For confidentiality reasons, the number of funds is not published.

Table C8: Australian Prudential Regulatory Authority (APRA) regulated superannuation funds — Distribution by fund balance in 2014-15[a]

Decile [b]	Fund balance range	Number of funds claiming excess franking credits	Percentage claiming excess franking credits	Average excess franking credits claimed ($)[c]	Total excess franking credits claimed ($m)[d]
1[e]	$0	174	50.1%	29,929	5.2
2	$1 to $101,068	165	76.7%	854	0.1
3	$101,069 to $205,401	243	86.5%	1,687	0.4
4	$205,402 to $309,472	267	94.7%	2,777	0.7
5	$309,473 to $458,968	252	89.7%	4,057	1.0
6	$458,969 to $650,510	252	89.7%	5,671	1.4
7	$650,511 to $981,296	247	87.6%	6,985	1.7
8	$981,297 to $1,634,549	252	89.7%	11,815	3.0
9	$1,634,550 to $4,851,537	240	85.4%	20,823	5.0
10	$4,851,538 and over	94	33.5%	3,033,446	285.1
Total APRA-regulated superannuation funds		**2,186**	**77.7%**	**138,973**	**303.8**

(a) Figures may not sum to totals due to rounding.
(b) Based on the fund balance of all APRA-regulated superannuation funds in 2014-15.
(c) Calculated as the average franking credit refund of those funds who received a refund in 2014-15.
(d) Calculated as *the number claiming excess franking credits* multiplied by the *average excess franking credits claimed*.
(e) As around 12.3 per cent of APRA-regulated superannuation funds have zero fund balance, there is no meaningful way to separate these funds when grouping by fund balance. As a result, the first decile includes all zero balance funds, which are then subtracted from the second decile (which as a result only includes around 7.7 per cent of APRA-regulated superannuation funds).

Appendix C

About Chartered Accountants Australia and New Zealand

Chartered Accountants Australia and New Zealand is a professional body comprised of over 120,000 diverse, talented and financially astute members who utilise their skills every day to make a difference for businesses the world over.

Members are known for their professional integrity, principled judgment, financial discipline and a forward- looking approach to business which contributes to the prosperity of our nations.

We focus on the education and lifelong learning of our members, and engage in advocacy and thought leadership in areas of public interest that impact the economy and domestic and international markets.

We are a member of the International Federation of Accountants, and are connected globally through the
800,000-strong Global Accounting Alliance and Chartered Accountants Worldwide which brings together leading Institutes in Australia, England and Wales, Ireland, New Zealand, Scotland and South Africa to support and promote over 320,000 Chartered Accountants in more than 180 countries.

We also have a strategic alliance with the Association of Chartered Certified Accountants. The alliance represents 788,000 current and next generation professional accountants across 181 countries and is one of the largest accounting alliances in the world providing the full range of accounting qualifications to students and business.