Australian Shareholders' Association

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Director
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By email: frankeddistconsult@treasury.gov.au

AUSTRALIAN SHAREHOLDERS' ASSOCIATION – CONSULTATION ON TREASURY LAWS AMENDMENT (MEASURES FOR A LATER SITTING) BILL 2022: FRANKED DISTRIBUTIONS FUNDED BY CAPITAL RAISINGS

Dear Madam/Sir

The Australian Shareholders' Association (ASA) represents its members to promote and safeguard their interests in the Australian equity capital markets. The ASA is an independent not-for-profit organisation funded by and operating in the interests of its members, primarily individual and retail investors, self-managed superannuation fund (SMSF) trustees and investors generally seeking ASA's representation and support.

Thank you for the opportunity to submit comments to the *Consultation on Treasury Laws Amendment (Measures for a later sitting) Bill 2022: Franked distributions funded by capital raisings* (exposure draft).

ASA supports existing laws which prevent franked distributions in certain circumstances associated with tax avoidance or manipulation of the franking system, receiving the benefits of franking. We support measures to address intentional tax avoidance or manipulation of the franking system with intent to avoid tax.

We have a number of concerns regarding the proposed legislation in regard to the potential impact on holders of exchange traded securities, especially retail shareholders.

They include its retrospective nature, the broadness and potential subjectivity of the tests to determine which transactions have been captured and the administrative and financial burden for individuals who inadvertently fall foul of the legislation and must amend tax returns potentially dating back six years.

It is proposed the legislation will apply retrospectively in line with the announcement in the Government's 2016-17 Mid-Year Economic and Fiscal Outlook. ASA does not support application of any new law on a retrospective basis.

We consider it will be unreasonable and unfair to expect retail shareholders to somehow anticipate which transactions may be captured by the broad application of the tests within this legislation, transactions they have no control over. Where the shareholders are in pension phase of self-funded retirement this is likely to increase the complexity and stress of managing the portfolio through the amendment phase.

We consider the application of the test to determine whether the amendments apply to be unreasonably subjective and broad.

We question how consistency with "the established practice of the entity of making distributions of that kind on a regular basis" will be assessed in practice. We note shareholders should also be able to confidently classify the distribution in the relevant tax year.

Companies are not homogenous and while some pay similar dividends year in and year out, many don't. Some will be on a growth path or reaching maturity where they are generating franking credits and commencing a dividend paying practice – the initial dividends may be captured. Other companies pay dividends that vary with earnings, and cashflow. Will companies that have been cautious and reduced dividends in the face of COVID-19, and then resumed paying dividends in subsequent period, be captured when dividends restart – or will that only occur if the payment is more than the "expected" annual dividend and paid out of usual timing?

Similarly, the assessment of principal purpose or effect test for a capital raising assumes all companies will operate in a linear fashion, and that earnings can be retained on balance sheet until paid in dividends. It ignores the experience where excess "lazy" capital and cash on a balance sheet attracts hostile takeovers, so it's best for companies to reduce their capital when they have no immediate need for it. It ignores the need to raise capital through new shares when the share price is high, when the use for the capital is most attractive for investors. It ignores the time to reinvest earnings in new ventures, equipment or working capital is dictated by the business.

There is also no clarity on how long after a capital raising might a dividend be paid without being captured by the legislation.

The unintended consequences of too broad and subjective tests, where the assessment outcome may seem arbitrary, may be for companies to favour funding dividends with debt. And for retail shareholders to concentrate their investments even further in the regular dividend paying companies.

We also flag potential difficulties for superannuation funds with large numbers of beneficiaries to manage subsequent changes to franking credit status of dividends in the year or two following its receipt. This is due to the pooled nature of the fund and members joining and departing throughout the year. Any retrospectivity will be even more complex on the beneficiaries.

We suggest the legislation should not be made retrospective. It should make clear the circumstances which will be captured, and the period where a capital raising will be

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considered to be funding the payment of a franked dividend. It should convey how a company that does not pay consistent dividends can avoid being captured by the legislation. Although we note capital raisings and dividend announcements are usually timed to coincide with the release of financial results to ASX so would expect them to take place in a "similar period". We expect listed companies will need to seek rulings from ATO and communicate those to shareholders when raising capital while paying franked dividends in order to assist the shareholders to manage their affairs appropriately.

Retail shareholders may be building their wealth and/or saving for retirement. The legislative framework and detail need to acknowledge the transfer of the risks associated with longevity and sustaining retirement incomes to individuals with the rise of compulsory superannuation. The laws associated with owning shares, which include taxation legislation, need to be clear and easily understood by individuals. Any change to legislation needs to be easy to navigate for individuals especially those who may be older and navigating the pension phase of self-funded retirement.

If you have any questions about these comments or other matters, please do not hesitate to contact me (ceo@asa.asn.au), or Fiona Balzer, Policy & Advocacy Manager (policy@asa.asn.au).

Yours sincerely

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