Franked distributions and capital raising

OVERVIEW

As part of the 2016-17 Mid-Year Economic and Fiscal Outlook, an integrity measure was announced to prevent the distribution of franking credits where a distribution to shareholders is funded by particular capital raising activities.

The Government has prepared exposure draft legislation giving effect to this measure, which will prevent companies from attaching franking credits to distributions to shareholders made outside or additional to the company's normal dividend cycle, to the extent the distributions are funded directly or indirectly by capital raising activities that result in the issue of new equity interests.

PURPOSE OF LAW

The prosed law is intended to add distributions funded by capital raising to the list of distributions that are unfrankable.

It attempts to delineate between separate decisions to change the gearing within a company by raising equity and franked dividend payment decisions, while capturing tied or related decisions where a capital raising at head entity or subsidiary level was substantially motivated to convey the franking benefit.

SCOPE

This position will apply to ASA submissions and responses to request for consultation.

POSITION

- Companies should strive to distribute franking credits to Australian resident shareholders within the constraints of the company's balance sheet and cash requirements for investment.
- 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.
- ASA does not support application of any new law on a retrospective basis.
- The risks associated with longevity and sustaining retirement incomes were transferred 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.

ASA CONCERNS

Does this only cover questionable raisings, or will it capture sensible circumstances?
Will applicability be apparent at the time of the capital raising and dividend (established practice test is likely to subjective for all but a few companies)?
Will in specie dividends be captured?
Will legislation drive increased debt levels to ensure no inadvertent capture of a transaction?

Relevant ASA positions
[ASA Voting and engagement guideline 16]
[ASA Submission Terms of Reference Retirement Income Review (15 August 2019)]
[Alliance (joint) Submission to Retirement Income Review (4 February 2020)]

Position approved by ASA Policy Committee 29 September 2022