Objection to the Possible Abolition of Franking Credits

As you are aware, currently there is a review of the taxation system. There is a rumour that the commission is looking at recommending the abolition of imputation credits for shares. (Refer an article by respected financial advisor Noel Whittaker in the Brisbane Sunday Mail dated 05 April 2009).

Is the rumour true?
If so, is the plan a misguided money grabbing exercise by a greedy government thinking about the short benefit to the government's financial woes without any intelligent thought about the long term consequences of double taxing company profits?
Or
Is it a deliberate attempt to ensure that most, if not all, current and future retirees are dependent on government pensions that we all know the government will not be able to afford?

Current treatment would indicate that the government is against self funded retirees.
Is the current government against self funded retirees?

By way of background I supply the following:

Over the last 20 years or more we have been warned that because of our aging population and increasing percentage of elderly retirees, the government will not be able to afford to pay all of those retirees a pension. We were all encouraged to provide for ourselves by investing in superannuation; so much so that compulsory superannuation was introduced for every working Australian. The 9% compulsory contribution is really not enough and it should be more like 15%, but it is a good start. I personally believe that it is in the country's and the individual's best interest that every working Australian be given the maximum encouragement possible to be fully self funded in their retirement, thereby not being a financial burden on the Australian community or government.

Imputation credits are not a gift. Imputation credits are recognition by the Australian Tax Office that a company has paid the appropriate level of taxation on their profit and that credit is available to be passed onto the company shareholder to offset against the shareholder's taxable income, thus ensuring that the company profit is not double taxed.

As a self funded retiree, the abolition of imputation credits will mean largely a reduction of 30% of the share based income of my superannuation fund which in turn will have a dramatic negative effect on my standard of living. I am not alone. Many thousands of other self funded retirees will also be adversely affected. Many of us may be forced to apply for old age pensions simply to survive. That strikes me as poor policy.

The abolition of imputation credits will have far bigger, negative long term effects on every working Australian who is a member of a superannuation fund now and into the future.
Currently, superannuation funds pay 15% tax on income and contributions during the saving or contribution phase.
As an example, if a company pays a franked dividend of $70.00 it comes with a $30.00 imputation credit. To evaluate the tax payable, the dividend and credit are added together ($100.00) and taxed at 15% ($15.00). The $15.00 tax is then offset by the $30.00 imputation credit and the superannuation fund receives a tax refund of $15.00 because of the tax already paid by the company. The net after tax return to the superannuation fund is $85.00.
If imputation credits are abolished and the tax on superannuation funds remain the same, the superannuation fund will receive an after tax return on the same dividend of $59.50. ie an income reduction of 30%.
Even if tax on superannuation fund earnings was abolished, the net after tax return on the same dividend would be $70.00. ie an income reduction of 17.65%.
In either case, the long term effect on superannuation funds will be dramatic. Because of the compound effect of interest, reduced income reinvestment and time the retirement benefit available to the superannuation fund account holder will be substantially reduced. With someone just entering the work force now, they could expect their retirement benefit to be less than half what would otherwise have been the case with the existence of franking credits. The retirees may then have insufficient money to fund their retirement and be forced to access a government pension.

The effect of abolishing imputation credits will not stop there. Because share investments without imputation credits will produce lower after tax returns they will be a less desirable investment and, due to the age old principle of supply and demand, the value of shares will decline with a consequent decline in the current value of superannuation fund holder's accounts. The value of superannuation fund holder's accounts have been savaged by the GFC. They certainly do not need to be savaged again by poorly thought out government policy.

That is not the end if it. Because share investments without imputation credits would be seen as less desirable, investors would be less likely to invest in new share offerings, thereby reducing the level of funding available for corporate growth and expansion. Would the companies like Wesfarmers, Bluescope, Commonwealth Bank and others that recently went to the market for additional funding to support their balance sheets have been given the support that they received had it not been for franking credits?

Years ago, because of double taxation of company profits, business could not grow with the result of over investment in housing and under investment in shares. We were becoming the best housed third world country in the world.
If imputation credits are abolished, that is where we are headed together with a grossly under funded, progressively increasing, ageing population.