It has been reported that there is a proposal to scrap the dividend imputation system in order to reduce company tax to 19% thereby making investment in Australia more attractive to overseas investors. Dividend imputation was introduced by the Keating government as a quid pro quo for the introduction of capital gains tax. Prior to these initiatives companies and shareholders alike did not look favorably on dividends which were taxed twice, once in the hands of the company and again in the hands of the shareholder with the combined rates as high as 84%. Shareholders preferred that companies retained earnings which would increase the value of the company and shareholder rewards would be in the form of tax free capital gains. The Keating initiatives were designed to increase the attractiveness of dividends. The two go together and if imputation is to be scrapped so too should the capital gains tax.

The introduction of the GST by the Howard government was designed to provide relief from crippling high personal marginal tax rates and also to eliminate a number of inefficient and inequitable State taxes. It was only partially successful, stamp duty, land tax and payroll tax (an obscenity in these times of increasing unemployment) remain. The GST however did allow the Howard government to introduce further reforms to the dividend imputation system to the great benefit of self funded retirees, low income earners with some share investments and any working Australian contributing to superannuation (virtually every employee in the country). As a self funded retiree who has never made any claims on Centrelink I vehemently oppose any initiative to scrap dividend imputation for the following reasons.

1) It is inequitable that a dollar of earnings is taxed twice, once in the company's hands and once in the shareholder's.

2) The proposal would provide benefits to overseas investors at the expense of Australian investors, especially workers saving through superannuation, self funded retirees and low income earners with some shareholdings. It is these groups who benefit much more from the imputation system than high income earners.

3) For years I have listened to the exhortations of financial gurus to have a significant proportion of an investment portfolio in overseas shares as the Australian market represents only 2% of the world market and many profitable industries do not exist here. I have resisted these urgings largely because of the dividend imputation system but if this were to be abolished I would shift the major part of my investments overseas. I am sure many others, both individuals and institutions, would do likewise. This could result in a massive outflow of capital from the country, perhaps balanced by inflows from overseas which would mean that more and more Australian companies would be foreign owned.

4) The proposal would result in a reduction in the amount collected by the Medicare levy. Franked dividends are grossed up in the individual's hands and the levy is based on the grossed up amount. Companies don't pay the Medicare levy, individuals do.

5) Self funded retirees and superannuation funds have suffered massive dimunition in the value of their assets due the global financial crisis. Dividend imputation abolition would give up to a 30% reduction in an already diminished income. More and more retirees would be claiming Centrelink benefits which the Government would find increasingly difficult to fund. This would apply both to present and future retirees.

6) The attractiveness of owning Australian shares, at least for Australians, would be greatly reduced which could precipitate further large falls on the Australian Stock Market.

In summary scrapping dividend imputation would produce tax inequities, result in transfer of benefits from Australians to foreigners, impact low and middle income earners the most and face the Government with a big increase in Centrelink payments.

Yours etc, John K Geary
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