



## THE TAX INSTITUTE

THE MARK OF EXPERTISE

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14 April 2014

General Manager  
Law Design Practice  
The Treasury  
Langton Crescent  
PARKES ACT 2600

By email: [taxlawdesign@treasury.gov.au](mailto:taxlawdesign@treasury.gov.au)

Dear Mr Leggett,

### **Preventing Dividend Washing**

The Tax Institute welcomes the opportunity to make a submission to the Treasury in relation to the *Tax and Superannuation Laws Amendment (2014 Measures No. 2) Bill 2014: Preventing distribution washing (Exposure Draft)*.

#### **Overview**

While we agree that dividend washing schemes threaten the integrity of the imputation system, we do not believe that they require the introduction of a specific integrity provision. The anti-avoidance provision in section 177EA of the *Income Tax Assessment Act 1936* should be sufficient to address this issue, particularly given the Commissioner's view on its application in the recently publicised Draft Taxation Determination TD 2014/D1.

Nevertheless, if it is the Government's view that a specific integrity provision is warranted, we would suggest changes to the Exposure Draft to ensure that it does not capture legitimate transactions on the cum-dividend market.

#### ***Application of existing anti-avoidance provision***

We consider that the existing anti-avoidance provision in section 177EA is suitable for addressing dividend washing schemes. The introduction of a specific integrity provision will add unnecessary complexity to the tax law and add to the existing legislative backlog in respect of announced but unenacted tax measures.

We refer to our earlier submission dated 17 June 2013 in response to the Treasury Discussion Paper "Preventing dividend washing" in which we supported the implementation of a targeted solution to address dividend washing alongside the

operation of the anti-avoidance rules. At the time of drafting that submission, the Commissioner had not applied the general anti-avoidance rules to dividend washing and had issued private binding rulings noting that, in similar circumstances, section 177EA would not apply.

The Commissioner has since issued Draft Taxation Determination TD 2014/D1 confirming that Part IVA could apply to dividend washing arrangements. Based on our discussions with the ATO in relation to this Draft Taxation Determination, we understand that it will be finalised shortly without significant changes.

We understand that the Commissioner is firmly of the view that Part IVA applies both before and after the date that the Draft Taxation Determination is finalised, and compliance activity has commenced in this regard with letters sent to approximately 3000 taxpayers. Accordingly, we do not see any indication that requiring the Commissioner to make a Part IVA determination in respect of each dividend washing scheme would result in an unnecessary burden on the ATO.

Furthermore, the Explanatory Memorandum to the Exposure Draft at paragraphs 1.22 and 1.63 indicates that Part IVA could be applied to such schemes, even in low value cases of less than \$5,000 of franking credits in a year which are exempted from the draft provision.

### ***Issues with targeted measure***

Notwithstanding the above, if it is the Government's view that a specific integrity provision is required to combat dividend washing, we note that the issues below with respect to the Exposure Draft.

The exception for low value cases in section 207-157(3) offers little comfort to individuals who are small holders as the Explanatory Memorandum indicates that Part IVA could nevertheless apply to such cases.

The Exposure Draft at section 207-157(1) does not specify a timeframe between the purchase of the "washed interest" and the sale of the "substantially identical interest". This could be interpreted as capturing purchases on the cum-dividend market years after the sale of the ex-dividend interest. As the provision does not look to the intention behind the transactions, and purchases on the cum-dividend market could be made for commercial purposes, the failure to specify a short timeframe of approximately 3 days could capture legitimate transactions.

The Exposure Draft at section 207-157(1) captures disposals of interests by the member or a 'connected entity'. The Explanatory Memorandum states that there is no requirement that the member and the connected entity even be aware of each other's actions: paragraph 1.49 of the Explanatory Memorandum. The concept of "connected entity" in the current tax law at section 995-1 *Income Tax Assessment Act 1997* refers to the definition of 'associate' in section 318 of the *Income Tax Assessment Act 1936*

which is broad and complex to navigate. The inclusion of trades by connected entities, together with the flexibility of the concept of a “substantially identical interest”, and the lack of a specified timeframe, could capture legitimate commercial transactions.

We also suggest that you carefully consider the impact of this integrity provision on charities.

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If you would like to discuss any of the above, please contact either me or Tax Counsel, Thilini Wickramasuriya, on 02 8223 0044.

Yours sincerely

A handwritten signature in black ink, appearing to read "M. Flynn", followed by a long, horizontal, slightly wavy line.

Michael Flynn  
President