Understanding share dividends and dividend imputation

Client Fact Sheet

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Dividends from Australian companies are distributed to investors after companies have paid tax on their profits. Under the dividend imputation system (which helps to avoid double taxation of company profits), investors receive a tax credit for the amount of tax that the company has already paid on the original profits. The system works as follows:

If a company makes a profit of $1000 which is fully taxable, it pays tax at the current company tax rate of 30% which equates to tax paid of $300, leaving $700 available for distribution. If there are 10 shareholders, each receives an after-tax dividend of $70, with a $30 franking credit. Since the profits associated with the dividends have been fully taxed, the after-tax dividends are said to be fully franked. However, there are situations when this is not the case, and dividends can have partial or no franking.

For the purposes of our illustrations, we have assumed that dividends are fully franked.

For after-tax dividends, the grossed up amount (that is the shareholder's share of the pre-tax profit) must be included in the shareholder's tax return as assessable income. In this example, the grossed-up dividend amount is $100 ($70 plus the $30 company tax paid with respect to that dividend). However, a franking credit of $30 also applies.

In this example, the effect of the credit is that if the shareholder's marginal tax rate is equal to 30% no tax will be paid on the dividends. If the marginal tax rate is less than 30%, this may result in a tax credit which could be used to offset other tax payable, Medicare levy, or be received as a tax refund.

Shareholder's marginal tax rate	45%	30%	15%
Franked Dividend paid	70	70	70
Plus imputation credit (representing company tax paid)	30	30	30
Assessable Income	100	100	100
Tax Assessed Less: Franking Credit	45 (30)	30 (30)	15 (30)
Tax payable	15	Nil	Nil
Excess credit to be offset against other tax payable/receive as a refund	Nil	Nil	15
Net dividend received	55	70	70

(excluding Medicare levy and flood levy)

Dividend imputation thus provides tax-effective income, where the dividend comes from investment in tax-paying companies, either directly or through a unit trust or master fund. For example, a retiree on a marginal tax rate of 15% (excluding Medicare levy) can receive dividends with no tax liability and can also use franking credits to offset Medicare levy, tax payable on other income, e.g. interest income, or receive as a refund.

An example:

A retired person receives $70 as a fully franked dividend with a credit of $30. Total tax payable is $15 (15% of $100) but franking credits reduce this tax to zero.

In addition, the retiree has an excess franking credit of $15 ($30 - $15). Therefore, if $200 income from a fixed interest investment is also received, the $30 tax liability is reduced to only $15 by using the $15 credit.

Need more information?

If there's anything else you need to know, please call your financial adviser, or our dedicated Customer Service team on 13 11 55 and ask for 'Super' between 8am and 6pm (Eastern Standard Time) Monday to Friday. We'll be happy to help.

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