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The New Zealand Productivity Commission
BY EMAIL:
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Dear Sir / Madam

Mutual Recognition of Imputation & Franking Credits

We write in response to the Australia and New Zealand Productivity Commissions' consideration of the mutual recognition of imputation and franking credits.

SUMMARY

The question as stated in the issues paper released in April 2012 by the Productivity Commissions is as follows:

What would be the costs and benefits of mutual recognition of imputation credits? (Question 28)

For Nuplex, the benefits of mutual recognition are summarised below:

- The mutual recognition of imputation and franking credits will increase the after tax return on Nuplex's shares for shareholders. This should result in a higher market capitalisation, giving rise to consequential benefits from a capital markets perspective.
- Mutual recognition provides the opportunity for Nuplex to offer competitive share-based remuneration packages allowing the company to attract top talent. This will also allow for improved movement of that talent between Nuplex's Australian and New Zealand businesses which will enhance the diffusion of best practices.
- Both of these points are consistent with Treasury's current perspective on improving the flow of *capital* across the Tasman, and its view on the direction of Closer Economic Relations ("CER") in respect of the movement of *labour*.

NUPLEX'S BACKGROUND

Nuplex is a global leader in the manufacture and distribution of resins and associated speciality products, with an especially strong presence in the Australasian region. The company is listed on both the ASX and NZX with approximately 80% - 90% of its shareholders being New Zealanders.

Of the \$1.6 billion of revenue derived in the 2011 financial year, 38% was derived from Australia and 11% was derived from New Zealand.¹

Accordingly, trans-Tasman business accounts for approximately half of Nuplex's sales.

¹ Nuplex 2011 Annual Report, page 2

MUTUAL RECOGNITION RESULTING IN AN INCREASE IN AFTER TAX RETURNS FOR SHAREHOLDERS

In March 2012, Gabriel Makhoulf, the Secretary to the Treasury, speaking to the International Fiscal Association in Queenstown noted that:

We also recommend mutual recognition of imputation credits with Australia. This would promote freer flows of capital across the Tasman and would extend to capital the trans-Tasman single economic market that largely operates for goods, services and people.

Mutual recognition of imputation credits is a growth enhancing strategy for both New Zealand and Australia.²

Nuplex agrees with this view. As noted in the background section above, approximately 38% of Nuplex's sales are derived from Australia, yet 80% - 90% of its shareholders are New Zealanders. Accordingly, the recognition in New Zealand of franking credits generated in Australia on those sales would increase the after tax returns for New Zealand investors. This is illustrated in further detail in Appendix 1.

This is consistent with the view of Treasury which noted in its October 2008 issuer paper:

The fact that trans-Tasman investment needs to generate a higher pre-tax return implies investment inefficiencies. By removing this bias, mutual recognition would increase the productivity of investment within Australia and New Zealand and boost our international competitiveness.³

The increased returns to shareholders from mutual recognition should result in a higher market capitalisation for Nuplex, which should bring additional benefits from a capital markets perspective, namely:

- An improvement of Nuplex's credit rating which will lower its cost of borrowing; and
- Enhance Nuplex's ability to raise equity through future rights issues.

Both points will result in an improved ability to raise capital for the expansion of Nuplex's business which will allow it to create more jobs and earn additional foreign currency. In addition, the expansion of business activity will increase Nuplex's contribution to the New Zealand tax base.

MUTUAL RECOGNITION RESULTING IN ENHANCEMENTS TO SHARE-BASED REMUNERATION

Share-based remuneration packages have become more prevalent in recent years. Looking ahead, for Nuplex to compete with other employers for top talent, it will need to be in a position to offer competitive share-based remuneration packages. Mutual recognition of imputation and franking credits provides the opportunity for Nuplex to offer such packages which will provide the following benefits to Nuplex:

- Allow the company to attract top talent when competing with other employers; and
- Improve the movement of that talent between Nuplex's Australian and New Zealand businesses which will enhance the diffusion of best practices.

This is consistent with Treasury's perspective on CER when it noted that:

*Over the years, CER has evolved to focus more strongly on removing barriers behind the border – not just barriers to free flows of goods and services, but also seeking to facilitate flows of factors of production such as capital and **people**⁴.(emphasis added)*

² 'The New Zealand Economy and Tax Policy' Speech delivered by Gabriel Makhoulf, Secretary to the Treasury, The International Fiscal Association, Queenstown, 17 March 2012

³ 'Mutual Recognition of Franking Credits and New Zealand Imputation Credits: A New Zealand Submission to the Australia's Future Tax System Review' New Zealand Treasury, October 2008 at page 9

In addition, a deeper participation by executives in Nuplex's equity will allow for improved alignment between personal rewards and business performance which should correlate to an improvement in Nuplex's results.

GOING FORWARD

Should you have any questions going forward please feel free to contact us.

Yours sincerely

Ian Davis
Chief Financial Officer

⁴ 'Mutual Recognition of Franking Credits and New Zealand Imputation Credits: A New Zealand Submission to the Australia's Future Tax System Review' New Zealand Treasury, October 2008 at page 10

Appendix 1

Total Dividends paid in the 2008 to 2011 Financial Years		
	Without mutual recognition	With mutual recognition
Total dividends distributed	127,142,000	127,142,000
Total franking credits distributed	43,245,171	43,245,171
Dividends distributed to NZ shareholders (approx. 85% of total)	108,070,700	108,070,700
Franking credits distributed to NZ shareholders (approx. 85% of total)	36,758,396	36,758,396
New Zealand Shareholders		
Dividend received	108,070,700	108,070,700
Franking credit recognised	0	36,758,396
Taxable income	108,070,700	144,829,096
Shareholder tax on taxable income at 33%*	35,663,331	47,793,602
Less franking credit	0	(36,758,396)
Final tax liability	35,663,331	11,035,206
*Notes: Proxy median rate for the 2008 - 2011 Financial Years		