# TAX TALKS

Australia's Tax News Podcast - The Podcast for Australian Tax Professionals

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## 262 | Declaring a Dividend

Declaring a dividend happens in 5 steps.

**Declaring a Dividend**

It feels business as usual. Declaring a dividend is something every accountant does after finishing the books of a profitable year.

But it is actually not that straight forward. There are 5 steps to run through. And heavy penalties if you get this wrong.

### Five Steps

To declare a dividend you go through five steps: 1 – Eligibility Test; 2 – Payment Terms; 3 – Declaration; 4 – Documentation; 5 – Payment or Journal Entry.

### Step # 1 – Eligibility Test

Before you can declare a dividend, you must be satisfied that the company is eligible to even declare a dividend. The company must pass the following five tests, which are:

1 – Net Assets Test – The company has sufficient net assets.
2 – Fairness Test – The dividend is fair and reasonable to shareholders;
3 – Prejudice Test – The dividend does not prejudice creditors;
4 – Profits Test – The company has sufficient profits; and
5 – Constitution Test – The company's constitution is met.

Every company must pass these tests. So in a corporate group you still need to run through these on a company-by-company basis. See ep 260 for more details about these tests.

### Step # 2 – Payment Terms

The replaceable rule in s254U CA gives directors the power to decide whether a dividend is payable or not and to determine the amount and payment date of a dividend.

Most company constitutions say the same, although some constitutions might require shareholder approval for the payment of a dividend.

The company's directors need to decide whether the dividend will be just determined to be paid or actually declared. And if declared when payment is due.

When you declare a dividend, the company incurs a liability to its shareholders right then and there at the time of declaring the dividend. And the directors can no longer easily revoke this decision.

However, when you only determine to pay a dividend, the company does not yet incur a liability. The directors just determine to pay at such and such date. There is no debt until that date passes. And the directors can revoke this decision at any time before the actual payment.

And so it is a lot more common nowadays to just determine to pay a dividend rather to actually declare a dividend. However, many older constitutions still have a requirement that the dividend be ‘declared’.

**Step # 3 – Declaration**

The directors need to actually declare (or determine to pay) the dividend. And they do this in a directors meeting.

This meeting must take place before the dividend is actually paid out. This will become important when we talk about Div 7A dividends in ep 261.

**Step # 4 – Documentation**

The director’s decision to declare (or determine to pay) must be documented in minutes and these minutes must be noted in the company’s register.

See example of those minutes below.

**Step # 5 – Payment or Journal Entry**

And then the dividend is paid out or recorded through a journal entry as stipulated in the minutes of the directors meeting.

**EXAMPLE**

Here is an example of minutes for a dividend payment.

**Sample Pty Ltd**
ABN 123 456 789
**Minutes of Meeting of Directors**

Held at 123 Sample Street, Imagine VIC 3210
On 30 June 2022
Present Bill Smith (chairperson and director) and Sally Smith (director)
Nobody absent

**Minutes**

The chairperson reported that the minutes of the previous meeting had been signed as a true record.

The directors hereby resolve to recommend the payment of a dividend of $1,200 per share, so a total dividend of $120,000 given that there are 100 shares.

It was declared that the recommended dividend of $120,000 be franked to the extent of 25%.

There being no further business the meeting then closed.

Signed as a true record

[Electronically Signed]

Bill Smith
Chairperson

## MORE

Eligibility Test for Dividend Payments

Div 7A Dividends

The Eichmann Case

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