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3 April 2017
Australia 2017/05

Tax Insights

Corporate tax rate resolved (for now)

On Friday 31 March, 2017, almost a year after the 2016-17 Federal Budget announcement, the deal was done. *Treasury Laws Amendment (Enterprise Tax Plan) Bill 2016* was passed with amendments by the Senate. The Bill still needs to return to the House of Representatives (when Parliament resumes in May) to be passed by the House and receive Royal Assent.

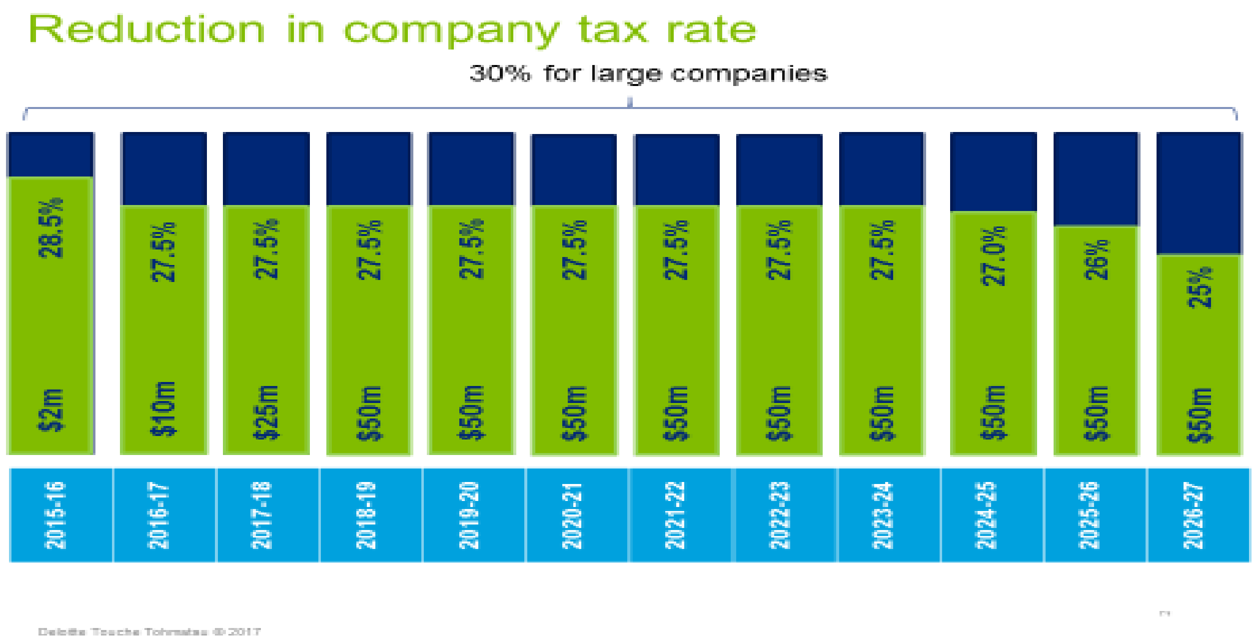
The end result: a staged reduction in the corporate tax rate for companies with an annual turnover of less than $50 million.

Stage 1 (as it is now called) rate cut

Currently the company tax rate is 28.5 percent for companies with a turnover of less than $2 million and 30 percent for all other companies. The amended legislation finally agreed in the Senate under a crossbench deal is to:

- Reduce the small company tax rate to 27.5% for the current year (2016-17);
- Progressively lift the small company turnover threshold for these purposes to $50 million;
- Lower the company tax rate to 25% for such companies over a ten year glide path; and
- Leave the company tax rate at 30% for all other companies.

To access the reduced rates, the company must carry on a business. Turnover is based on worldwide ordinary income, including that of affiliates and entities connected with the company (irrespective of their residency).



	2015-16	2016-17	2017-18	2018-19	2024-25	2025-26	2026-27
Company tax rate (%)	28.5	27.5	27.5	27.5	27	26	25
Turnover threshold	$2 m	$10 m	$25 m	$50 m	$50 m		

The Treasurer has made a statement of support for the amended Bill which is expected to allow the ATO to implement the measures agreed by the Senate. This means that the ATO will anticipate the tax rate change for affected taxpayers in the final quarter PAYG instalment for June 2017.

The government estimates that 883,000 companies earn up to $50 million in turnover. These companies together with unincorporated businesses employ 6.5 million Australians.

The ALP's position on retaining the measures for companies with a turnover of less than $50 million is yet to be finalised.

Companies with an annual turnover of $50 million or over will pay tax at 30% on the whole of their taxable income as usual, under what is now a two-tier tax system for companies.

Rate cut prospects for big corporates (or Stage 2)

The Government has stated that it remains "absolutely committed" to the full plan of tax cuts. However Stage 2 will be presented to the Senate only when the Government is in a position to believe that the Bill will pass. This means that large companies have little certainty on where the company tax rate will land.

Implications for franking

The rate change can, by legislative design, result in a trapping of franking credits. This trapping of franking credits may potentially arise for each pool of companies that, over time, move to the lower tax rate as the scope of companies eligible for the lower company tax rate increases over time.

Companies are required to determine the maximum franking credit by reference to the company tax rate for imputation purposes, which is essentially the expected current year corporate tax rate. So if a company paid tax at 30% during prior years, but has an expected current year corporate tax rate of (say) 27.5% (that is, its relevant turnover is less than the relevant company threshold for the current year), then in that current year, it franks its dividends using 27.5% notwithstanding that the relevant prior year profits were taxed at 30%.

Companies subject to the tax rate change should review their franking and retained profits position as soon as possible in order to consider their dividend strategy.