

**JULY 2017**

**TAX ALERT: SBE REDUCED TAX RATES FOR PASSIVE INVESTMENTS?**

***Introduction***

The Treasury Laws Amendment (Enterprise Tax Plan) Bill 2016 was introduced into Parliament on 1 September 2016 and contains a number of changes to progressively reduce the corporate tax rate for small business entities and the franking of dividends which apply

Effective from 1 July 2016, new rules were introduced to progressively reduce the corporate tax rate for “small business entities” (or **SBEs**), which are limited to corporate tax entities which satisfy two requirements:

- (a) carrying on a ‘business’; and
- (b) having aggregated turnover below the ‘aggregated turnover threshold’.

The following table provides a summary of how the progressive reduction in the corporate tax rate will be rolled out.

Income Year	Aggregated turnover	Company tax rate
2016	< \$2 million	28.5%
2017	< \$10 million	27.5%
2018	< \$25 million	
2019	< \$50 million	
2020		
2021		
2022		
2023		
2024		
2025		27%
2026		26%
2027 & Later		25%

Importantly, these new rules to reduce corporate tax rates for SBEs were not designed to apply to any corporate entities which hold passive investments (such as rental properties), as they could not satisfy the first eligibility requirement of “carrying on a business”.

***ATO Releases Draft Tax Ruling***

In March 2017, the ATO released draft Taxation Ruling TR 2017/D2, which deals with the issue of the central management and control test to establish residency for corporate entities.



Interestingly, within the footnotes of the draft ruling, the ATO stated that:

*“Generally where a company is established or maintained to make a profit or gain for its shareholders it is likely to carry on business..... This is so even if the company only holds passive investments, and its activities consist of receiving rents or returns on its investments and distributing them to shareholders.”*

At face value, these comments may mean that investment companies are carrying on a business. However, it is important to recognise the context of the information, it was included within the footnotes of a draft ruling on the unrelated topic of tax residency.

### ***Recent News Reports***

Yesterday, news reports declared that the Australian Taxation Office (ATO) has broadened the interpretation of company tax reductions for SBEs.

Some of the major news outlets published articles claiming that the ATO may have opened the floodgates for family investment companies to claim back millions of dollars in company tax, after issuing the (draft) ruling.

Until the draft ruling was issued in March, it had been understood that Australia’s many passive investment vehicles, used mainly by families and investors to take advantage of a corporate tax rate lower than marginal income tax rates, would not be entitled to the recent rule changes to reduce corporate tax rates for SBEs.

### ***Government Response***

Revenue Minister Kelly O'Dwyer responded to news reports that “... the policy decision made by the Government to reduce the tax rate for small companies was not meant to apply to passive investment companies.”

The Minister also reiterated that the ruling was still in draft form and it was "premature" to suggest eligibility for lower rates had been broadened.

The ATO has indicated it is working on more detailed guidance on the issue, which should be published “very soon”.

### ***LLCA Comment***

We consider that it is always important to consider announcements relating tax issues in the correct context. In this instance, we are considering information from a footnote within a draft tax ruling, addressing an entirely different tax issue.

When the ATO releases clarification on this issue shortly, we will see how the ATO interprets the ‘carrying on business’ requirement in the context of the company tax rate reductions and then we consider the potential application of these rules against specific circumstances.

***Please do not hesitate to contact your Lowe Lippmann Relationship Partner if you wish to discuss any of these matters further.***



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