Determining Your Company's Tax Rate

Form 1 July 2015, certain companies are eligible for a lower company tax rate than the standard 30% rate. The rules that apply for the 2016 and 2017 financial years are different to the rules that apply from the 2018 financial year onwards.

2016 and 2017 Financial Years

In the 2016 and 2017 years, companies that qualify as a Small Business Entity (SBE) are eligible for the lower company tax rates of 28.5% and 27.5% respectively.

A company qualifies as an SBE, if during the relevant year, it had:

- aggregated turnover of less than the relevant threshold (i.e. less than $2 million in 2016 and less than $10 million in 2017); and the company is “carrying on a business”.

According to the ATO, a company is likely to be considered to be carrying on a business where it “is **established and maintained to make a profit** for its shareholders, and **invests its assets** in gainful activities that have both a purpose and prospect of profit”

This means that a company is carrying on a business where it derives at least $1 of passive income such as dividends, interest and rent from its investments.

2018 Financial Year Onwards

From the 2017/18 financial year onwards, only companies that qualify as a **Base Rate Entity (BRE)** will be taxed at the lower company tax rate (e.g. 27.5%).

A company will qualify as a BRE in 2017/18 where its:

- aggregated turnover (worked out at the end of the financial year) is less than $25 million: and
- no more than 80% of the company’s assessable income for the year is Base Rate Entity passive income (BRE passive income).

BRE passive income includes interest, rents, dividends and franking credits, net capital gains, trust and partnership distributions to the extent they are referable (either directly or indirectly) to an amount that is otherwise passive income.

Where a company holds at least 10% of the voting power of another company (i.e. at least 10% of the ordinary shares), the dividends will not be BRE passive income.

Example 1

ABC Pty Ltd holds a commercial property that is leased on commercial terms and also derives income from the sale of products that it manufactures.

The company’s assessable income for the 2017/18 year consists of sales of $190,000 and BRE passive income (i.e. rent) of $810,000.

The company will qualify as a BRE as 19% (and not at least 20%) of its assessable income ($190,0000/$1,000,000) is BRE passive income.

Therefore the company will qualify for the 27.5% tax rate in the 2017/18 year.

Example 2

Assume the same facts except that sales are $210,000 and BRE passive income is $790,000.

In this situation, BRE passive income is 21% of the company's assessable income ($210,000/$1,000,000) which is more than 20%.

Accordingly, the company will not qualify as a BRE and will be taxed at the rate of 30%.

What company tax rate will apply in 2016?

In both examples, as ABC Pty Ltd has an aggregated turnover of less than $2 million, and is considered to be carrying on a business, the lower company tax rate of 28.5% will apply.

What company tax rate will apply in 2017?

In both examples, as ABC Pty Ltd has an aggregated turnover of less than $10 million, and is considered to be carrying on a business, the lower company tax rate of 27.5% will apply.

It would not matter if 100% of the company's assessable for the 2016 and 2017 years was passive income (i.e. rent) as the company would be considered to be carrying on business and therefore be entitled to the lower tax rate.