PCG 2017/D7 (Replaced) - Enterprise Tax Plan: small business over-franking in 2016-17 income year because of tax rate change

This draft Practical Compliance Guideline has been replaced by
PCG 2018/D5
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Enterprise Tax Plan: small business over-franking in 2016-17 income year because of tax rate change

Relying on this draft Guideline

This Practical Compliance Guideline is a draft for consultation purposes only. When the final Guideline issues, it will have the following preamble:

This Practical Compliance Guideline sets out a practical administration approach to assist taxpayers in complying with relevant tax laws. Provided you follow this guideline in good faith, the Commissioner will administer the law in accordance with this approach.

Table of Contents **Paragraph**

What this draft Guideline is about

1. If a corporate tax entity fully franked a distribution during its 2016–17 income year before the *Treasury Laws Amendment (Enterprise Tax Plan) Act 2017* (the amending Act) became law on 19 May 2017, the amount of the franking credit on the distribution statement provided to members may be incorrect. This is because the franked distribution would likely be based on the 30% corporate tax rate, when the entity's tax rate for that income year may in fact be 27.5% because of the law change.

2. This draft Guideline sets out a practical compliance approach that corporate tax entities may choose to use to inform members of the correct amount of franking credit attached to their distribution. The approach may reduce compliance costs for corporate tax entities by providing an alternative to seeking an exercise of the Commissioner's discretion to allow amendment of distribution statements.

Date of effect

3. This draft Guideline will have effect from the first day of an entity's 2016–17 income year.

Who this draft Guideline applies to

4. This draft Guideline applies to corporate tax entities where:

   (a) they have paid a fully franked (or close to fully franked) distribution at the corporate tax rate of 30% during the period of their 2016–17 income year before the law change on 19 May 2017 and

   (b) the distribution was over-franked as their corporate tax rate was reduced to 27.5% for their 2016–17 income year, because of the changes in the law.

5. This draft Guideline may also be relevant to members who have received a franked distribution (as detailed in paragraph 4 of this draft Guideline) from a corporate tax entity that had its corporate tax rate reduced to 27.5% for its 2016–17 income year.

Background

6. The amending Act amends the *Income Tax Rates Act 1986* to reduce the corporate tax rate for small businesses with an aggregated turnover of less than $10 million to 27.5% for their 2016–17 income year.

7. The maximum franking credit entitlement for a member is determined by applying the formula in section 202-60 of the *Income Tax Assessment Act 1997* (ITAA 1997). Under this section, the corporate tax rate is used to calculate the maximum franking credit for a distribution.

8. During their 2016–17 income year, companies may have made fully franked distributions and calculated the maximum franking credit on the basis of the 30% tax rate, rather than the amended 27.5% tax rate. In these cases, the distribution statement provided to the member will contain an incorrect amount of franking credit. Notwithstanding the amount stated in the distribution statement, members will be entitled only to a franking credit calculated by reference to the 27.5% tax rate (see section 202-65 of the ITAA 1997).

Compliance approach

Written notification informing members

9. For the 2016–17 income year, a corporate tax entity to which this draft Guideline applies may inform its members of the correct franking credit to which they are entitled under the revised corporate tax rate in writing without reissuing the distribution statement.

10. The Commissioner will not impose penalties on the corporate tax entity for giving a member an incorrect distribution statement provided it gives written notice to each of its members clearly showing the correct amount of the franking credit. The notice should be provided in the same way as the distribution statement was provided (which may be electronically by email).

11. The corporate tax entity can provide this notice to their members without seeking an exercise of the Commissioner's discretion to allow amendment of the distribution statement.

12. The notice should indicate that the distribution statement previously provided was incorrect and should contain the following details:

   (a) name of the entity making the distribution

   (b) date on which the distribution was made

(c) amount of the distribution

(d) revised amount of franking credit allocated to the distribution, rounded to the nearest cent

(e) franking percentage for the distribution, worked out to two decimal places

(f) amount of any withholding tax deducted from the distribution

(g) name of the member.

13. The members must use this to correctly report on their tax return.

14. The corporate tax entity should adjust its franking account to reflect the fact that the franking debit to the account should be calculated by reference to the 27.5% corporate tax rate.

Amended distribution statement

15. Alternatively, the corporate tax entity may apply to the Commissioner for permission to amend the distribution statement under section 202-85 of the ITAA 1997.

16. If the Commissioner grants permission, the corporate tax entity would then be able to provide the member with a new distribution statement and no penalty would be imposed for the initial incorrect statement.

Example

1. *ABC Co pays a fully franked distribution to a member of $100. The distribution was made on 31 December 2016 before the law change. Applying the 30% tax rate, the company calculates the franking credit to be allocated to the distribution as $100 x 0.30/(1-0.30) = $42.86.*
2. *ABC Co provides a distribution statement to the member that states that the franking credit on the distribution is $42.86.*
3. *Subsequently the law change occurred which reduced the corporate tax rate for small businesses with an aggregated turnover of less than $10 million to 27.5% for their 2016–17 income year.*
4. *Instead of seeking an exercise of the Commissioner's discretion to allow an amended distribution statement, ABC Co sends a letter to each of its members containing the details set out in paragraph 12 of this draft Guideline, and explaining that the distribution statement was incorrect.*
5. *When members lodge their tax return, they will be able to use the information in this letter to determine the maximum franking credit on the distribution based on the 27.5% tax rate. Using section 202-65 of the ITAA 1997, this would be calculated as $100 x 0.275 / (1-0.275) = $37.93.*
6. *No penalty is imposed by the ATO.*

Commissioner of Taxation
22 May 2017

Your comments

17. You are invited to comment on this draft Practical Compliance Guideline including the proposed date of effect. Please forward your comments to the contact officer by the due date.

Due date: 6 June 2017

Contact officer details have been removed.

References

ATOlaw topic(s)	Income tax ~~ Assessable income ~~ Dividend income Income tax ~~ Capital management ~~ Franking credits / tax offsets
Legislative references	ITAA 1997 ITAA 1997 202-60 ITAA 1997 202-65 ITAA 1997 202-85 Income Tax Rates Act 1986 Treasury Laws Amendment (Enterprise Tax Plan) Act 1997
ATO references	1-BI6T26I
BSL	Individuals