Unlock 'trapped franking credits' with a solvent liquidation

Do you have a client at risk of missing out on valuable franking credits in their company?

Corporate tax rates for Base Rate Entities have reduced over recent years and currently sit at 25% for FY2022.

The maximum franking rate that a company can utilise is determined by the tax rate applicable to the financial year that dividends are paid. Any dividends paid in FY2022 will therefore have a maximum franking rate of 25% for Base Rate Entities (BRE) - even though the company may have historically paid tax at 30%.

For a BRE – those with turnover less than $50m and/or passive income[1] less than 80% of assessable income – **this could mean the franking credits generated from paying tax in previous years become 'trapped'**.

Below is a summary of the applicable tax rates:

	FY2020	FY2021	FY2022
Base Rate Entity	27.5%	26%	25%
Other company (Turnover is > $50m &/or passive income is > 80% of assessable income)	30%	30%	30%

[1] Income not derived from actively being involved in a business – for example Interest; Rental income; Royalties; Dividends (except non-portfolio); and Net Capital Gains.

Level 3, 431 King William Street, ADELAIDE SA 5000
t. 08 7202 1800
e. info@cliftonhall.com.au
w. www.cliftonhall.com.au

With the reduction in tax rates, **up to 22% of available franking credits can therefore become trapped** (based on FY2022 rates) and can't be passed on to shareholders, as shown below:

Tax rate	30%	27.5%	26%	25%
Franking Credit	$30.00	$26.55	$24.59	$23.33
Lost Franking Credit ($)	-	$3.45	$5.41	$6.67
Lost Franking Credit (%)	-	11.5%	18%	22%

Shareholders may then have to fund the shortfall between the available franking credits and their marginal tax rate.

However, a Members' Voluntary Liquidation (MVL) may provide a solution. The MVL is a solvent winding up of a company that can offer many taxation and other benefits by distributing assets in specie, including the avoidance of stamp duty on land transfers.

The MVL can also access the trapped franking credits and pay dividends at the historical 30% rate, subject to the available balance of franking credits. Once a company is in liquidation, it ceases to be a BRE, thereby reverting back to the 30% rate and unlocking available franking credits.

Clifton Hall has a wealth of experience in MVL appointments and assisting companies and their advisors with tax-effective solutions, including winding up subsidiaries in complex group structures. The MVL is relatively inexpensive and easy to initiate, but can provide significant benefits to shareholders.

As always, there's no cost or obligation in meeting or discussing your client's circumstances with us – or just send through a balance sheet to start the discussion and identify available options.

For more information, or a brochure on the process to discuss with clients, please contact any of Tim Clifton, Mark Hall, Daniel Lopresti or Simon Miller on 08 7202 1800.

Level 3, 431 King William Street, ADELAIDE SA 5000
t. 08 7202 1800
e. info@cliftonhall.com.au
w. www.cliftonhall.com.au