Large business 45

Large business

For tax purposes, large businesses are generally defined as those entities with total income, as shown on their income tax return, of $10 million or more. Superannuation funds with total investment income of $50 million or more are also classified as large businesses. In addition, all public companies not operating as bodies corporate and all subsidiaries of large businesses are classified as large businesses, regardless of their total income.

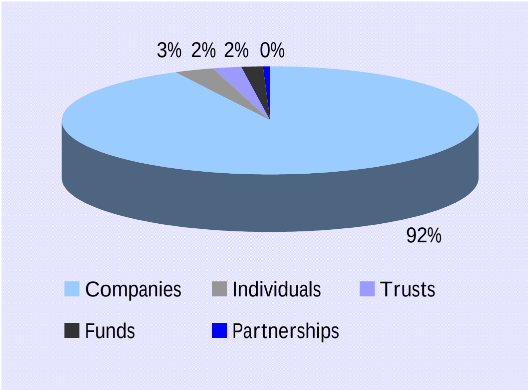
Within the ATO, large businesses are clients of the large business and international (LB&I) line. Individuals are clients of large business and international if they have gross income greater than $10 million. Individuals with a gross income of less than $10 million are also clients of large business and international if they have non-primary production business income derived from a partnership or trust that has been defined as a large business. An individual has non-primary production business income if they have any distributions or deductions from partnerships and trusts.

The statistics in this chapter are compiled from tax returns for the 1998–99 income year. The last section on the petroleum resource rent tax, however, is based on data for the 1999–2000 financial year. Detailed information on specific types of large businesses, including applicable tax rates, are presented in the chapters on companies, funds, and partnerships and trusts.

Client population

In 1998–99, 30 958 tax returns were lodged by large business and international clients. Companies accounted for 92% of the total large business and international client population, yet represented only 5% of all companies. The remaining 95% of companies were clients of the small business (SB) line (see table 6.1).

Figure 5.1: Composition of the LB&I client population[1]



1. A proportion of 0.0% indicates a proportion of less than 0.05%.

The geographic distribution of large business and international taxpayers reflects the dominance of Sydney and Melbourne as the major business centres of Australia. In 1998–99, 46% of large business and international returns were lodged in New South Wales, with a further 23% lodged in Victoria and 13% lodged in Queensland.

Industry

In 1998–99, the largest proportion (47%) of large business and international clients who stated

Table 5.1: LB&I clients by state[1] and entity

State	Individuals	Companies	Funds	Partnerships	Trusts	Total[2]
	no.	no.	no.	no.	no.	no.
NSW	362	13 301	280	66	139	14 148
Vic.	265	6 522	192	33	178	7 190
Qld	146	3 644	28	13	55	3 886
WA	97	2 700	29	13	48	2 887
SA	72	1 666	20	7	37	1 802
Tas.	17	303	7	5	5	333
NT	6	155	5	0	5	164
ACT	13	202	9	0	5	226
Not stated	0	127	0	9	186	322
Total[2]	**978**	**28 620**	**566**	**142**	**652**	**30 958**

1. Refers to the state in which LB&I clients lodged their returns, which may not be where all their business activities were conducted.
2. Components may not add up to totals as some cells containing a value of 5 can represent any number between 1 and 5.

Table 5.2: LB&I clients[1] by industry[2]

Industry	Individuals	Companies	Partnerships	Trusts	Total
	no.	no.	no.	no.	no.
Finance, insurance, real estate & business services	18	12 746	64	169	12 997
Manufacturing	5	3 291	7	23	3 323
Wholesale trade	5	3 279	5	37	3 322
Retail trade	5	1 809	19	99	1 932
Mining	0	1 332	5	5	1 339
Construction	0	1 076	12	18	1 106
Transport & storage	5	885	5	5	892
Accommodation, cafes & restaurants	0	740	5	8	749
Primary production	58	529	5	12	602
Cultural & recreational services	7	463	5	5	477
Personal and other services	5	299	0	5	303
Health & community services	5	253	6	9	270
Communication	0	182	0	5	184
Property	5	0	5	167	174
Electricity, gas & water supply	0	144	5	5	146
Education	0	52	0	5	53
Total industry stated[3]	**99**	**27 080**	**132**	**558**	**27 869**
Industry not stated[4]	879	1 540	10	94	2 523
Total	**978**	**28 620**	**142**	**652**	**30 392**

1. Excludes funds.
2. The industry groups are coded using the Australian and New Zealand Standard Industrial Classification system. Prior to 1995–96, the Australian Standard Industrial Classification system was used. Therefore, it is not possible to do any long time series analyses for industry because the industry groups are not comparable.
3. Components may not add up to totals as some cells containing a value of 5 can represent any number between 1 and 5.
4. Includes those LB&I individuals that have only registered a subsidiary return income from partnerships and trusts and registered as salary and wage earners.

their industry, were in finance, real estate and business services industry. This trend is partly due to the large number of holding companies included in this category. Some of these holding companies are involved in the in-house financial operations of firms within a corporate structure that can be involved in non-financial activities, such as manufacturing, mining and similar activities. Companies account for 98% of the total number of large business and international clients in the finance, insurance, real estate and business services industry.

The manufacturing and the wholesale trade industries accounted for the second largest proportion (12% each) of large business and international clients. Approximately 97% of large business and international clients who stated their industry, were companies.

Income

The income, expenditure, profitability and level of tax payable by a large business depends to a large extent on the characteristics of the industry in which the business operates. The performance of businesses within a particular industry may be influenced by factors such as:

- the industry life cycle;
- the economic/business cycle;
- the level of competition within the industry;
- the age of the firm;
- the threat of new entrants;
- the level of regulation in the industry;
- the emergence of substitutes;
- technological changes;
- policy changes; and
- changes in tastes and/or preferences within society.

In 1998–99, large business and international clients accounted for less than 1% of all income tax returns lodged. However, they accounted for 65% of total income, 33% of taxable income.

Nearly all large business and international clients are companies (92%). These companies accounted for 96% of large business and

Table 5.3: LB&I clients' income by entity

	Total income[1]	Taxable income	Net tax
	$m	$m	$m
Individuals	853	825	141
Companies	968 509	132 591	15 507
Funds	38 651	20 365	2 146
Partnerships[2]	3 519	n.a.	n.a.
Trusts[2]	8 111	n.a.	n.a.
Total[3]	**1 008 013**	**153 781**	**17 794**

1. For individuals, total income includes net business income (or loss), distributions from partnerships or trusts, and non-business income such as interest, dividends, and salary and wages.
2. Profits from partnerships and trusts are distributed to partners and beneficiaries respectively who pay tax on their income.
3. Total income does not include partnerships and trusts total income because their income is distributed to the other entities as taxable income.

international clients' total income, and 86% of taxable income.

In 1998–99, resident large business and international companies had an average total income of $40.2 million, while non-resident large business and international companies had an average total income of $25.5 million. Similarly, resident large business and international companies had a higher average taxable income ($10.1 million) compared to non-resident large business and international companies ($5.4million). However, resident large business and international companies had lower average net tax payable ($1.3 million) compared to non-resident large business and international companies ($2 million).

Expenses

The major types of expenses for large business and international clients varied according to industry and entity type. In 1998–99, companies accounted for 96% of total expenses claimed by large business and international clients. The main type of expense claimed was cost of sales (48%), followed by interest expenses (9%).

Net tax

Partnerships and trusts do not generally pay tax in their own right. Partnerships distribute their net income (or loss) to the partners who include their share in their income tax returns. Trusts distribute their income to beneficiaries who include the income in their tax returns. If no beneficiary is, at the time, entitled to a trust distribution, or if the beneficiaries are entitled to a distribution but are under a legal disability (for example, a minor), then the trustee is liable to be assessed on the trust's net income.

In 1998–99, large business and international clients were liable for $17.8 billion in net tax. Most of this liability was incurred by companies (87%). Funds were liable for a further 12% while individuals were liable for nearly 1% in net tax.

While large business and international companies made up only 5% of all companies, they were liable for 72% of all net tax payable by companies. Large business and international funds made up less than 1% of all funds, yet were liable for 68% of all net tax payable by funds.

Table 5.4: LB&I clients'[1] expenses by entity

Type of expense[2]	Individuals	Companies	Partnerships	Trusts	Total
	$m	$m	$m	$m	$m
Cost of sales	11	407 577	2 290	6 346	416 224
Interest	2	73 802	406	382	74 592
Depreciation	2	21 222	177	152	21 553
External labour	0	19 944	705	557	21 206
Superannuation deductions	0	4 927	40	118	5 085
Rent	1	9 512	138	276	9 927
Repairs & maintenance	1	8 639	66	92	8 798
Royalty	n.a.	3 752	68	101	3 921
Lease payments	0	3 830	80	54	3 964
Motor vehicles	0	2 741	9	40	2 790
Bad debts	0	2 975	17	10	3 002
Other	17	274 743	14 932	3 302	292 994
Total	**33**	**833 664**	**18 929**	**11 430**	**864 056**

1. Excludes superannuation funds.
2. Where zero amount is reported, amount is less than $0.5 million.

Large business and international clients accounted for less than 1% of all income tax returns lodged, but they accounted for 19% of all net tax payable.

Ratio analysis

Five ratios have been calculated for large business and international companies at the broad industry level. These ratios provide an insight into the operations of large companies and show any similarities and/or differences between industries. There are many factors that can create differences in the values of these ratios. Varied legislative measures, industry structure and individual business operations can all influence the level of the ratios. It should be noted that the ratios are averages across each industry and, as such, may be influenced by, and tend to mask, the companies that have values at the extremes.

Table 5.5 shows that the financial ratios vary between industries—this is particularly true for interest cover ratio and effective rate of tax ratios. For example, the effective rate of tax varies from between 16% for the manufacturing industry to 32% for the education and wholesale trade industries.

One ratio that stands out is the high interest cover ratio for the education industry. This ratio is high because their interest expenses are quite low. This is caused by balance sheet structures that differ from those used by non-government entities, due to the availability of non-commercial borrowing conditions.

Definitions

Return on assets: operating profit or loss, plus interest costs, divided by total assets. This measures the ordinary economic return that accrues to a business from their assets. Interest expenses are netted out from operating profit so that the calculation focuses on the ordinary returns of the assets and ignores how the assets are financed. Average asset levels vary across industries. Service-based businesses generally have very low asset levels, while mining and manufacturing operations are more heavily based around capital equipment. This ratio depends on how the assets themselves are valued.

Net profit margin: operating profit or loss, minus tax payable, divided by sales. It relates after tax profit to sales revenue. Profit margins vary across industries with many large retail operations having high volume, low margin business, whereas other industries may operate with lower volumes and higher margins.

Gearing: total liabilities divided by shareholder funds. It reflects the borrowing position of the firm compared to its equity. In general, higher levels of gearing lead to higher interest cost deductions and lower tax paid. In essence, some of the profit from the geared company or group is transferred to the lending entities.

Interest cover ratio: operating profit or loss, plus interest costs, divided by interest costs. This ratio shows the proportion of operating profit that is required to cover the interest expenses of the business. Higher borrowings lead to greater interest expenses and so the ratio measures the capacity of a business to service the interest component of debt capital.

Effective tax rate: the tax payable, divided by the operating profit or loss. This ratio shows the proportion of a firm's operating profit that is paid in tax. It is important to note that there are numerous reconciliation items (capital gains, legislative concessions, losses and the like.) that are applied to operating profit before tax is calculated. The use of these reconciliation items will affect the value of the ratio.

Petroleum resource rent tax

Large business and international also has responsibility for the petroleum resource rent tax. This tax is imposed by the *Petroleum Resource Rent Tax Act 1987* on all offshore petroleum projects except the North-west Shelf. It is calculated at the rate of 40% of taxable profit, which is the excess of assessable receipts over deductible expenditure and transferred exploration expenditure. The tax is paid to the ATO on a quarterly basis. The first three payments are made in October, January and April. Companies submit their tax return in August and a final payment, or refund, is made at that time.

In the 1999–2000 financial year, the petroleum resource rent tax totalled $1.2 billion—exceeding budget estimates by 64%. Two main factors contributed to this better than forecast result: oil prices were much higher for the period than forecast in the May 1999 Budget, and the Longford oil refinery (which had suffered reduced production as a result of damages in 1998) was repaired sooner than expected, allowing a full return to production from Bass Strait.

Table 5.5: LB&I companies[1]: financial ratios by industry

Industry	Return on assets[2]	Net profit margin	Gearing	Interest cover ratio	Effective rate of tax
	ratio	ratio	ratio	ratio	%
Primary production	0.12	0.11	1.25	6.30	22.56
Mining	0.15	0.28	1.30	6.59	23.08
Manufacturing	0.13	0.12	1.75	7.07	16.07
Electricity, gas & water supply	0.14	0.22	3.57	5.04	16.76
Construction	0.14	0.06	3.07	15.40	27.03
Wholesale trade	0.10	0.03	1.58	5.56	32.20
Retail trade	0.16	0.02	2.14	3.01	27.86
Accommodation, cafes & restaurants	0.09	0.07	1.02	11.42	23.74
Transport & storage	0.10	0.08	2.20	6.65	25.65
Communication	1.57	0.24	1.50	11.45	17.45
Finance, insurance, real estate & business services[3]	0.10	1.83	4.11	2.38	11.15
Education	0.08	0.08	4.49	134.89	32.47
Health & community services	0.16	0.12	1.94	11.37	27.48
Cultural & recreational services	0.09	0.19	1.94	4.73	27.31
Personal & other services	0.12	0.08	1.24	6.21	24.48
Industry not stated	0.09	0.13	2.02	10.88	23.15
Total	**0.11**	**0.22**	**3.22**	**2.95**	**14.93**

1. All loss making companies have been excluded.

2. Return on assets is calculated before tax and therefore excludes net tax.

3. Finance, insurance, real estate and business services is a very diversified sector. It is worth noting that the four major banks all have a higher effective rate of tax than the average.

Detailed tables

The following detailed tables on large business and international clients can be found on the CD-ROM attached to this publication.

Table 1: Large business individuals: selected items by industry

Table 2: Large business companies: selected items by industry

Table 3: Large business funds: selected items

Table 4: Large business partnerships: selected items by industry

Table 5: Large business trusts: selected items by industry

Table 6: Large business individuals: selected items by grade of net tax

Table 7: Large business companies: selected items by grade of tax payable

Table 8: Large business individuals: selected items by grade of total income

Table 9: Large business companies: selected items by grade of total income

Table 10: Large business companies: financial ratios by industry