



Tax Transparency Report

2022-2023

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1. Introduction

Australian Foundation Investment Company Limited ("AFI" or "AFIC") is a Listed Investment Company as defined in the Income Tax Assessment Act 1997 s115.290.

AFIC is listed on the Australian Securities Exchange and the New Zealand Securities Exchange (code "AFI") and its shares may be purchased or sold via a broker. Full details regarding the Company's corporate history, Board & Management, Corporate Governance, Financial Statements and Annual Reports and dividend payment are available via its website afi.com.au

AFIC through its Board and Investment Committee manage the Company's portfolios of investments. It has an arrangement with Australian Investment Company Services Limited (an entity in which AFIC has a 75% share) to provide administrative and operational services.

Listed Investment Companies (LIC) which make capital gains upon which tax is payable on the sale of investments held for more than one year are able to attach to their dividends a LIC capital gains amount which some shareholders are able to use to claim a tax deduction. For more details, see the Company's Annual Report.

As a listed company with over 160,000 shareholders, AFIC is fully compliant with Principle 6 of the "ASX Governance Principles" in respecting the rights of security holders. As part of that, the Board of AFIC maintains that this includes being transparent about the taxation affairs of the Company.

The Board has therefore determined that AFIC should publish a Tax Transparency Report in accordance with the Voluntary Tax Transparency Code as developed by the Board of Taxation and released as part of the Federal Budget in May 2016.

As AFIC is a Listed Investment Company with operations only in Australia, it has no international related party dealings or offshore financing or tax concessions.

Shareholders and other stakeholders should be aware that AFIC was part of the ATO's Combined Assurance Review for the income years ended 30 June 2018, 30 June 2019, 30 June 2020 and 30 June 2021 (2018, 2019, 2020 and 2021 income years). They found that AFIC paid the right amount of Australian income tax for the relevant years, and that they had a high level of assurance over AFIC's management of its tax risks.

The previous review covering the 2014 to 2016 tax years had also confirmed that AFIC had paid the right amount of tax and that the ATO had a high level of assurance over AFIC's management of tax risks.

The Directors confirm that, to the best of their knowledge and belief, the Company continues to have effective policies and processes in place to manage tax risk.

2. Approach to Tax Strategy and Governance

Tax Strategy & Governance

The Board has a formal policy in place with regards to taxation strategy. This is disclosed below :

“The Board of Australian Foundation Investment Company Limited (“AFIC”) seeks to meet its obligations with regards to current and future taxation on its activities in a manner that maintains its reputation as a responsible and secure vehicle for its shareholders’ funds.

AFIC will prepare tax returns and disclose its tax positions based on its, and its advisers’, interpretation of current taxation legislation and consistent with ATO guidance, where applicable.

AFIC’s strategy is to provide an optimal outcome for its shareholders consistent with its stated goals. This by necessity will not involve utilising high-risk taxation-driven strategies.

Unless a range of taxation outcomes are specifically provided for under the legislation (e.g. parcel selection for Capital Gains Tax), if there is a possibility that a transaction or range of transactions could be taxed in different ways, or if there is a difference of views, AFIC will aim to record the transaction in a conservative manner consistent with legislation and ATO guidance. If significant uncertainty exists, management will seek external advice in writing and document and present such advice.

Management and their advisers will inform the Board either directly or through the Audit Committee when such a disparity of outcomes exists, whilst being mindful of materiality and reputational risk.

GST and other indirect taxes such as FBT, SGC and withholding tax legislation will be complied with to the fullest extent possible, and after consultation with external advisers where appropriate. Where the payment of such taxes is managed by outsourced agencies, the Company shall review those taxes as part of its ongoing compliance procedures. Any errors in meeting obligations once discovered will be reported to the Audit Committee and remedied as soon as possible.

An independent tester (usually the AICS Internal Auditor) will conduct periodic tax controls testing of the tax corporate governance framework, including testing controls associated with the operational and compliance aspects of the company’s tax obligations (including income tax and indirect tax obligations). All key controls will be tested by the independent tester annually, including the following Board Level Controls (BLC) and Managerial Level Controls (MLC) as outlined in the ATO’s Tax Risk Management and Governance Review Guide and GST Governance, Data Testing and Transaction Testing Guide:

- BLC 3 – The board is appropriately informed
- MLC 1 – Roles and responsibilities are clearly understood
- MLC 3 – Significant transactions are identified
- MLC 4 – Controls in place for data (for GST testing only)
- MLC 6 – Documented control framework
- MLC 7 – Procedures to explain significant differences

The Board will make an annual statement in the Tax Transparency Report attesting that they have effective policies and processes in place to manage tax risk.

AFIC will meet its taxation obligations in a timely manner and will ensure that the policies, procedures and practices are maintained to meet this policy.”

A standing item on the Board Meeting Agenda allows Management to provide the Board with an update on taxation matters, consistent with the above policy.

In addition, the Board’s Audit Committee receives reports from the external auditor relating to the conduct of financial statement audits/reviews, which includes procedures performed by the auditor (see below) on material tax balances within the half-year and year-end financial reports.

As a LIC that invests primarily in Australian listed assets, the Company’s tax affairs are relatively simple, and relate to income tax payable on the distribution that it receives (whilst accounting for any attached franking credits) plus the net income from interest and option trading, and tax on the capital gains that it makes from its investments held on capital account. Much of the tax paid and franking credits received are passed onto AFIC’s shareholders in the form of franked dividends.

Taxation Risk Management

The Board of Australian Foundation Investment Company Limited is responsible for overseeing the operations of the Company and ensuring that a sound system of internal controls is in place for risk management purposes.

This includes taxation risk, which is defined by the Company as the risk that the Company takes a tax position that is not in accordance with its risk appetite and/or the risk that the amounts of tax due are incorrectly calculated, provisioned for and/or paid.

The Board receives assurances from the Managing Director and the Chief Financial Officer (“CFO”) twice yearly regarding the operation and effectiveness of the Company’s internal controls (see the Corporate Governance Statement available on the website).

The Board has approved the overarching risk appetite of the Company and is assisted in its risk management activities by the Audit Committee. Coordination of risk management activities, including taxation risk, is done by the Chief Financial Officer, who reports to the Audit Committee on such matters.

The Risk Management Framework is reviewed by the Audit Committee on an annual basis, and such a review has been carried out this financial year. The framework has been developed to take into account the principles and guidelines outlined in AS/NZS ISO 31000: 2009 Risk Management – principles and guidelines. This approach involves establishing the context in which it operates, identifying the risks, analysing those risks, evaluating the risks, treating the risks where appropriate and monitoring, reviewing and reporting risks and the overall performance of the framework.

AICS as the provider of administrative and operational services to the Company has its own risk management processes and controls, including taxation risk and taxation policies and procedures. The efficacy of these internal controls is reported to the Company’s Audit Committee via an ASAE3150 report from the AICS internal auditor, Ernst & Young.

With regards to calculation of and provision for taxation, the Company notes the following controls that are in place to reduce the risk of material misstatement:

- Company’s tax returns are prepared by external advisers (PricewaterhouseCoopers, who are also the Company’s auditors).
- Company’s provisions for tax payable are reviewed twice a year by the auditors as part of the annual and half-yearly audit and review. This includes franking credit balances and LIC gain accounts.

- Company's auditors perform a review, on a sample basis, of the Company's capital gains in the year to attest to the accuracy of the record-keeping with regards to the tax cost-base of securities sold, and thus the amount of Capital Gains Tax incurred.

3. Reconciliation of Accounting Profit for the year ended 30 June 2023 to Taxes Payable at 30 June 2023

	2023 \$'000
Profit for the year before tax	330,755
Nominal tax at 30%	99,226
Less : net effect of franking credits on dividends received	(76,518)
Less : over provision in 2022	(1,499)
Less : sundry items not taxable but included in profit (e.g. net dividends receivable)	(665)
Total tax expense for the year per P&L	20,544
Add : Capital Gains Tax for Year on realised gains (incl. gains on revenue account)	25,622
Total tax charge 'incurred' for year including Capital Gains Tax	46,166
Less ; Foreign Tax Credits	(1,607)
Add : Sundry prior year items not included in profit	911
Less : PAYG tax for year already paid	(13,314)
Total tax payable per Balance Sheet at 30 June 2023	32,156

4. Effective Company Tax Rates

As per the figures in Section 3. above :

	2023 \$'000
Profit for the year before tax	330,755
Total tax expense for the year per P&L	20,544

Effective Tax Rate	6.2%
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These figures do not include the tax that has already been paid on the dividends that the Company has received. Franked dividends that AFIC receives are not free from tax. Instead, the tax (at 30%) has already been paid on the profits from which these dividends are sourced. It also does not include the effect of income that is required to be booked but is not taxable.

Imputation instead acts to ensure that these same profits are not taxed twice – by the company that paid the dividend to AFIC and then by AFIC itself or even three times – by the original paying company, by AFIC and then by the shareholder on receipt of a dividend from AFIC.

Including the imputation or franking credits, therefore, the effective tax rate would be as follows :

	2023 \$'000
Profit for the year before tax	330,755
Net effect of franking credits on dividends received as income	76,518
Foreign tax	1,607
Total tax expense for the year per P&L	20,544
Tax Expense including franking	98,669
Effective Tax Rate including franking	30%

This is equivalent to the prior year's figure which was also an effective tax rate of 30%.

5. Reconciliation of Taxes payable at 30 June 2023 to Taxes Paid for the 2022-23 year

	\$'000
Tax Payable as at 30 June 2023	32,156
Less : PAYG instalment subsequent	(477)
Less : Tax owed by subsidiary	(20)
Less : Income deferred and other adjustments per annual tax statements received after year-end from trusts that the Company invests in	(2,234)
Tax payable per Tax Return for 2022-2023	29,425

6. Total Taxes Paid Summary for the year ended 30 June 2023

As well as corporate income taxes paid, AFIC and its subsidiary AICS and their employees pay a number of other taxes.

AFIC's total tax contribution is summarised below :

	\$'000
Tax Payment per Tax Return	29,425
Tax paid in advance via PAYG (incl. July 2023)	13,278
Total corporate income tax paid	<u>42,703</u>
Tax pre-paid by companies that AFIC invests in received as franking credits on dividends	109,292
Foreign taxes paid (after tax-return adjustments)	1,570
Total corporate income tax borne by AFIC	<u>153,565</u>
Irrecoverable GST incurred by AFIC	562
PAYG on salaries withheld by AFIC Group	4,440
Payroll tax incurred by AFIC Group	283
Net GST collected by AFIC Group	229
Total tax contribution of AFIC for the 2022-23 year	<u>159,079</u>

7. Reconciliation of Accounting Profit for the Year Ended 30 June 2023 to Taxable Income

The accounting profit is not the same as taxable income due predominantly to the franking credits and foreign tax credits received, plus the adjustments to accounting income noted in Section 3.

	\$'000
Accounting Profit before tax per 2023 Annual Report	330,755
Less Profit of subsidiary (taxed separately)	(2,570)
Accounting profit of AFIC as taxable entity	<u>328,185</u>
Gains from investments on revenue account	8,958
Unrealised gain on trading portfolio	(1,410)
Net gains from investments on capital account	81,577
Income accounted for in past years and attribution income	27,932
Income not taxable in current year	(42,641)
Minor items taxable	(8)
Franking credits received	109,292
Taxable income	<u>511,885</u>
Tax payable at 30%	153,565
Tax paid overseas	(1,570)
Gross tax pre-paid by companies that AFIC invests in received as franking credits on dividends	(109,292)
Total tax paid or payable	<u>42,703</u>