US Tax Reform Initial thoughts on Global consequences

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US Tax Reform

	Current Law	House Blueprint	2016 Campaign	2017 Trump Plan
Corporate Tax Rate	35%	20%	15%	15%
Pass through rate	35% (Co) /39.6%	25%	15% (retained profit)	15%
Interest deductions	Allows	Eliminates net interest	US Manufacturers may elect interest or capital expense	Silent
Capital equipment	Depreciation	Immediate expense		Silent
Business concessions	Allows	Eliminates except R&D	Eliminates "most" except R&D	Eliminates "tax breaks for special interests"
Past foreign earnings	Deferral	8.75% on cash 3.5% on other	10% tax – cash 4% - other	One time tax – rate to be determined
Future foreign earnings	World wide	Territorial	World wide	Territorial
Border Adjustment Tax	-	Yes	Consider	Silent
Alternative Minimum Tax	Ind & Corp	Repeal Ind & Corp	Repeal Ind & Corp	Repeal Ind, silent Co
Individual tax brackets	7 with top 39.6%	12%, 25%, 33%	12%, 25%, 33%	10%, 25%, 35%
Cap gains & dividends	23.8%	50% exemption	New bracket rates	20%

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BAT: USD Appreciation

US Retailer 'R' sells a shirt for \$11.00, after purchasing it from Greece for 10 Euro*	Pre-BAT at 20% Tax Rate	BAT at Full "Theoretical" Appreciation of USD (25%)	BAT at 45% "Theoretical" Appreciation of USD (11%)		Pre-BAT at 35% Tax Rate	BAT at 91% of "Theoretical " Appreciation of USD (91%)
1 Euro equivalent in USD	\$1.00	80c	90c		\$1.00	81.5c
Sales (\$11.00)	11.00	11.00	11.00		11.00	11.00
Cost (Eur 10.00) in USD	10.00	8.00	9.00		10.00	8.15
Profit in USD	1.00	3.00	2.00		1.00	2.85
Tax - Profit (Conventional)	0.20				0.35	
Cashflow import cost denied		2.20	2.20			2.20
After tax profit	0.80	0.80	(0.20)		0.65	0.65

US impacts….uncertain… but following initial impressions (of GWJ) are:

1. The USD Appreciation would need to be between 91% and 100% of full "theoretical" appreciation for R to benefit from the tax cut to 20% in conjunction with a BAT. This is substantial and query whether it is realistic;

2. Note about 20%-30% of imports into the US are purchased in USD – so no initial FX benefit, pure cost;

3. Flow-on impact to higher prices and fall in demand as Big W passes on costs > US negative impacts > Inflation + higher interest rates

* Adapted from an example used by Prof Alex Raskolnikov, "A Tale of Two Tax Plans" in *Foreign Affairs*, July/August 2017

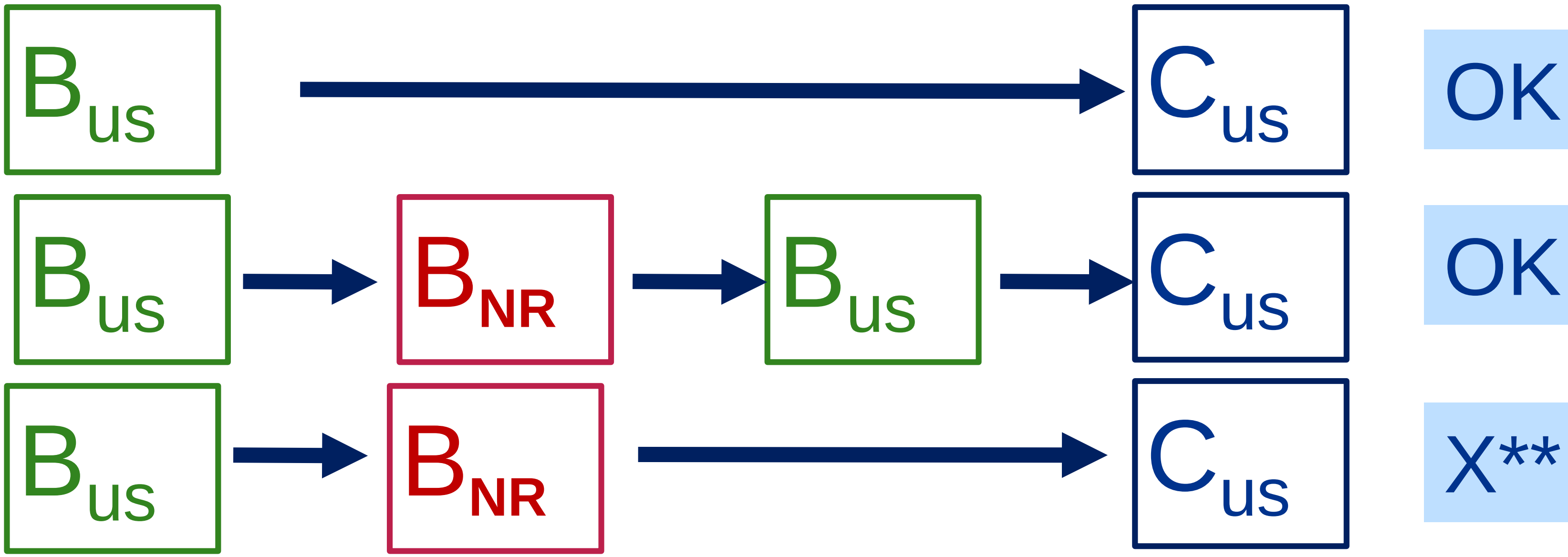
USD Appreciation - Global secondary impacts

International & Australian impacts:

1. Strong disincentive for US imports > **dislocation** for exporters to US
2. Cost reduction US exports if not full USD appreciation > competitors with US exporters **dislocation**
3. **Profit squeeze** USD appreciation for global businesses where USD costs and non-USD revenues
4. Asia – common for USD purchases & financing – capricious winners and losers > **dislocation**
5. Higher US inflation > higher US interest rates > higher global interest rates > **profit squeeze**
6. Faster search for alternative reserve currency to USD – **long term financial stability (?)**
7. Potential hedge fund activity to “short” developing country currencies > **potential high instability**

   Note China Tobin Tax in May 2016 with 0% rate

BAT: Non-resident business to US Consumers



** Need (a) Tariff, (b) De-facto VAT charge?, (c) Anti-avoidance rule, (d) Value-added rule or (e) Ban

Incentive for avoidance is much greater than corporate tax (profit) as based on cost of import

Global response: 1. Lift own tariffs in response

2. Non-US multilateral free trade agreements (eg. RECP, TPP-1)

3. Greater non-US bilateralism (eg. Mexico)

4. Ultra-focus on US supply chains because of high stakes (within & outside US)

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