

Alcoa of Australia Limited

2016 Tax Transparency Report



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Message from the Chairman and Managing Director

I am pleased to share this inaugural Tax Transparency Report for Alcoa of Australia Limited (Alcoa of Australia) which provides insight into the company's 2016 tax contributions and our approach to tax governance.

Publication of this report is aligned with our values - Act with Integrity and Operate with Excellence - and our open and transparent approach to business conduct.

This report builds on Alcoa of Australia's commitment to exemplary corporate governance as evidenced by the company's voluntary establishment of an Annual Compliance Arrangement with the Australian Tax Office (ATO) in 2012. It adopts all of the Australian Government's Board of Taxation's Tax Transparency Code recommendations for large businesses.

Alcoa of Australia and its subsidiaries recorded a net profit after tax of \$249.1 million for the 2016 income year. Income tax expense was \$148.7 million, resulting in an Effective Tax Rate of 37.4 per cent. Fully franked dividends of \$499.8 million were paid to shareholders in the 2016 calendar year.

These contributions are a significant part of the value Alcoa of Australia delivers to the Australian economy. More than 75 per cent of our total annual revenue stays in Australia through wages, local purchasing, taxes, royalties, capital investment and dividends to Australian shareholders.

I look forward to building on our successful 54-year history in Australia with a continued focus on delivering long-term sustainable outcomes.

Michael Parker
Chairman and Managing Director
Alcoa of Australia Limited

About Alcoa of Australia

Alcoa of Australia is an Australian entity with operations that represent one of the world's largest integrated bauxite mining, alumina refining and aluminium smelting systems.

Alcoa Australian Holdings Pty Ltd holds 60 per cent of the shares in Alcoa of Australia and Alumina Limited holds 40 per cent. Alcoa Australian Holdings Pty Ltd is ultimately 100 per cent held by Alcoa Corporation*, a company resident in the United States of America and listed on the New York Stock Exchange. Alumina Limited is an Australian company listed on the Australian Securities Exchange.

Alcoa of Australia's activities add value to Australia's local, state and national economies including approximately 4,300 direct jobs, predominantly in regional Australia.

Our principal operations include:

- Two bauxite mines in Western Australia (Huntly and Willowdale)
- Three alumina refineries in Western Australia (Kwinana, Pinjarra and Wagerup)
- One aluminium smelter in Victoria (Portland)**
- Two dedicated port facilities in Western Australia (Kwinana and Bunbury)



Alcoa of Australia mines approximately 32 million bone dry metric tonnes of bauxite, refines approximately nine million tonnes of alumina and produces some 300,000 tonnes of aluminium per annum.

We produce almost 43 per cent of Australia's alumina and approximately 20 per cent of Australia's aluminium. Our alumina production in Western Australia accounts for approximately eight per cent of total world demand.

* Alcoa Corporation became an independent, publicly traded company on 1 November 2016 when it completed the separation from its parent company Alcoa Inc. (now named Arconic Inc.). Please visit www.alcoa.com for further information.

** Portland Aluminium Smelter is ultimately held 55 per cent by Alcoa of Australia. Figures related to aluminium production represent 100 per cent of smelter output.

Approach to tax governance

Alcoa of Australia's approach to taxation is to meet all our tax obligations in full compliance with the law.

The Alcoa of Australia board of directors is responsible for ensuring that a sound system of internal controls is in place for tax governance purposes. The board receives assurances from the Managing Director and the Finance Director regarding the operation and effectiveness of the company's internal controls in relation to tax, including its tax management framework.

Alcoa of Australia's tax management framework is aligned with the ATO's Tax Risk Management and Governance Review Guide and includes the following key attributes:

- A fully resourced Australian tax function
- A formal self-assessment testing program for taxation in relation to roles, responsibilities, processes and systems, with external review by its auditors and reporting of test results to the board
- Use of external tax advisers to review tax returns and provide advice on material transactions
- Participation in the ATO's Annual Compliance Arrangement (discussed below)

Tax reviews are conducted in a conservative manner consistent with legislative requirements, utilising external expert opinions and ATO guidance where available.

Approach to engagement with the ATO

In 2012, Alcoa of Australia became the first company in Australia to voluntarily enter into an Annual Compliance Arrangement (ACA) with the ATO that covered all four taxes: income tax, Goods and Services Tax (GST), Fringe Benefits Tax and excise.

An ACA is premised on sound governance of tax risks and full disclosure when dealing with the ATO. It involves negotiating a joint 'terms of arrangement' which details the obligations of both the taxpayer and the ATO in regards to tax compliance.

Under the ACA, Alcoa of Australia commits to disclose material tax matters and uncertain tax positions to the ATO. Alcoa's Finance Director has provided the ATO with a declaration stating the company has strong corporate governance processes supporting tax compliance and confirms its tax management framework is aligned with the better practices set out in the ATO's Tax Risk Management and Governance Review Guide.

The period of the current ACA covers the periods ending 31 December 2016 or 31 March 2017 depending on the tax. Reviews of matters relevant to those periods are currently being conducted.

Tax contribution

During the 2016 income year, Alcoa of Australia paid \$370.4m in Australian federal and state taxes.

Table 1. Australian federal and state taxes paid during the income year ended 31 December 2016

| | |
|----------------------|------------------------|
| Corporate income tax | \$283.8 million |
| Employer taxes* | \$36.5 million |
| Royalties | \$50.1 million |
| Total | \$370.4 million |

*Includes fringe benefits tax and state based payroll tax

The amounts above exclude taxes collected by Alcoa of Australia and passed on to the ATO and state revenue offices, such as GST and Pay As You Go withholding on payments made to employees and contractors.

Corporate income tax paid during the year includes 11 instalments paid on 2016 profits, one final instalment paid on 2015 profits and remaining taxes due in respect of the lodged 2015 income tax return.

Disclosure to be made by Australian Tax Office

Each year the ATO discloses certain limited tax information for Alcoa of Australia. The disclosure for the income year ended 31 December 2016 will be made in December 2018 and is expected to be as follows.

Table 2. Expected ATO disclosure for the income year ended 31 December 2016

| | |
|----------------|-----------------|
| Gross income | \$3,416,237,867 |
| Taxable income | \$653,972,617 |
| Tax payable | \$190,786,992 |
| ABN | 93 004 879 298 |

Tax payable is taxable income multiplied by 30 per cent, reduced by research and development and foreign income tax offsets. This amount is different to the tax contribution in Table 1 because the 2016 tax payable was paid partly in 2016 and partly in 2017 under normal payment rules.

International related party dealings

One third of Alcoa of Australia's alumina sales, valued at \$1.18 billion, were made to Alcoa Corporation's subsidiaries. Alcoa Corporation's subsidiaries acquire alumina from many locations for processing into aluminium at its smelters globally or to market to third party customers. These sales are all made on normal commercial terms and conditions and at market rates.

There were also purchases and sales of other goods and services from and to Alcoa Corporation's subsidiaries as outlined in Table 3.

Table 3. Purchases and sales of goods and services from and to Alcoa Corporation's subsidiaries during the income year ended 31 December 2016

| | \$M | Nature of main product/service |
|---|------|--|
| Purchase of product from Alcoa Corporation | 53.8 | Raw materials |
| Purchase of services from Alcoa Corporation | 28.2 | Insurances, technical and management services, IT / transactional services, stock option recharges relating to shares issued to Alcoa of Australia employees |
| Services provided to Alcoa Corporation | 37.8 | Logistics, technical services |

These purchases and sales were made on normal commercial terms and conditions and market rates.

During the year all loans from related parties were repaid in full.

Both purchases and sales with related parties are reviewed by the ATO as part of the ACA arrangement. Business conducted between Alcoa of Australia and its shareholders is also governed by the Charter of the Alcoa World Alumina and Chemicals Strategic Council, which requires that such business be conducted on an arm's length basis.

Reconciliations of Australian accounting profit to tax expense and income tax payable

| Table 4. Reconciliations | 2016 \$M |
|---|---------------------|
| Operating profit / (loss) before tax | 397.8 |
| Prima facie tax expense (at 30%) | 119.3 |
| | |
| Amounts not recognised in profit but included in taxable income | |
| - Research and development concession | (1.1) |
| | |
| Amounts recognised in profit but not included in taxable income | |
| - Non-deductible entertainment expenditure | 0.2 |
| - Write down of book value of Portland Aluminium smelter | 12.5 |
| - Other | 1.4 |
| - Consumables, stores and spares inventory movement | 0.1 |
| - Difference between book and tax depreciation deductions for property, plant and equipment | 52.0 |
| - Difference between book and tax carrying values of trading stock and sundry inventories | 0.2 |
| - Provision for rehabilitation and closure cost movements | (2.4) |
| - Accounting for embedded derivatives | 1.0 |
| - Provision for employee benefit movements | (0.4) |
| - Utilisation of carried forward capital losses | (6.2) |
| - Write off of book value of capitalised exploration expenditure | 29.4 |
| - Difference between book and tax depreciation deductions for mine site capital expenditure | (0.8) |
| - Gas transportation costs - difference in book and tax accounting values | (2.3) |
| | |
| Current tax expense (income taxes payable for the current year) | 202.9 |
| Deferred tax expense | (54.2) |
| Income tax expense (as per income statement) | 148.7 |
| | |
| Income taxes payable | |
| Income taxes payable at beginning of financial year | 118.0 |
| Tax return adjustments and other | 7.0 |
| Less: income tax paid during the year | (283.8) |
| Income taxes payable for the current year | 202.9 |
| Income taxes payable as at 31 December 2016 | 44.1 |
| | |
| Accounting and Tax Transparency Code effective tax rate | |
| Income tax expense | 148.7 |
| Accounting profit before tax | 397.8 |
| Tax rate | 37.38% |