



MAY 2015

Welcome to the May 2015 Update

Taxation seems to still be the topic of discussion. The budget analysis article is lengthy and detailed, but well written and easily understood. It is recommended reading! Jon Daly's article about researching a company before investing is a reminder to all of us to do our homework.

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The 9 things you need to know before investing in a Company's shares

John Daly

There are 9 key areas Investors need to seriously think about before considering investing in a Company's shares. These will not carry equal importance for each investment being considered, but each will always be present and, as such, worthy of separate and detailed consideration.

1. What does the business do?

This is often a relatively easy question to answer - but not always - so it should never be taken lightly. For example Harvey Norman appears to be a retailer of electrical goods.

Upcoming Events



AIA Annual Investors Conference

Blackburn Discussion Group

3rd June 2015 7.15pm

Hills District Discussion Group

3rd June 2015 7.00pm

Brisbane Information Meeting

Colin Nicholson

3rd June 2015 1.30pm

For NSW Members -

One Day Course:

**How to beat the fund manager, -
Strategies for individual Investors**

12th June 2015

[Details](#)

The 9 things you need to know before investing in a Company's shares (cont'd)

Given that 88.7% of its profits last year came from 'Franchising Operations' and 'Property' however, it may more accurately be described as a franchisor and retail property investor. A clear understanding of the 'real business' of any Company is critical to understanding the next and possibly most important criterion.

2. How does it make money?

A deep appreciation of the company's business model, that is how it makes money, provides the underlying framework for assessing each of the other elements. Why is it so important? Let's look at two examples:

- a) Take companies whose profits are highly correlated with commodity prices, for example. Understanding the business models of two gold mining companies, one a high-cost producer and the other a low-cost producer, enables the investor to appreciate which is most likely to see the greater share price decline in a falling gold price environment.
- b) Leadership. A change in the leadership of a company is usually important, but all things being equal, it will be more important for a 'services' company than a 'manufacturing' company. For example a change in the CEO at Platinum Asset Management, one of Australia's most successful funds management businesses built by the current CEO Kerr Neilson, is likely to be significantly more important than a change in the CEO at Coca Cola Amatil, the Australian bottler of the world's most popular soft drink.

3. What is the Company's strategy?

Knowing how the Company intends to grow its business is crucial to understanding the likely (and possible range) of returns from an investment, as well as the time period over which it is anticipated these returns may be delivered.

For example, losses at Xero Limited increased by 95.8% in 2014 compared with the previous year. A failure to appreciate its strategy would immediately deem this a very poor result. However, during 2014 they also increased the size of their team by 53% - adding 403 people - to position themselves for a global marketing and sales assault in the years ahead. This aggressive strategy may not suit all Investors, but understanding it

is certainly crucial for those for whom it is appropriate – such as famous US venture-capitalist Peter Thiel.

4. What markets does the company operate in?

In order to gain a fuller appreciation for the possible upside' or 'downside' of an investment, it is important to understand the 'size of the pond' the company is fishing in. Not only is it important to understand the current size of the company's market(s), but also the relative positions of the current market participants as well as their likely trend – are they likely to expand or contract.

5. Who are its major competitors?

Identifying a Company's competitors is important primarily to answer the question posed above. If the Company I am looking to invest in wishes to grow its market share, how much of a fight are its competitors going to put up? It is also important to understand the possibility of corporate action within the sector. For example, the major competitors of Computershare in Australia are Link Market Services and Boardroom Limited. Both hold minor percentages of the share registry market compared to Computershare's dominant position. Is it likely that one or the other could be bought by Computershare? It is hard to be certain but more than probable that the ACCC would hesitate before such a deal went ahead.



6. What is the Company's history?

This is about the lessons that only experience can bring. An appreciation of where a business has come from in order to arrive at this point is critical to assessing how confidently the management is likely to move forward. A business that has just entered a new sector – without new technology providing give it a significant cost or feature advantage – is likely to face greater challenges than a seasoned operator.

7. Who is the team behind the business?

This point is highly correlated to the previous point. If the business has a long and successful history in its particular field and the people currently charged with its

stewardship have been at the helm for a long time – Investors can have a greater degree of confidence in management’s ability to navigate the vagaries of their industry than if a new team has recently arrived, all else being equal. This logic needs to be applied with caution, however, where an Investor is looking at a Company that needs to change – where management has become stale and fixed in the old ways of operating and where clearly ‘new ways’ are making significant inroads into their traditional markets. It is probably not unfair to use the impact internet advertising and businesses such as REA Group (www.realestate.com.au) and Carsales.com have had on the traditional classified advertising business of Fairfax Media as relevant examples.

8. What do the Company’s financials look like?

Of course, no investor will be surprised by the fact that we include ‘Financials’ in this list. While some investors will have a better appreciation for the details of financial information than others, having some understanding of the underlying drivers of profit is vital to ultimately forming an opinion as to the value of the company and its shares. Financial performance is related to how the company makes its money (factor 2) as well as the trend in performance (factor 3). This is especially important where this has been constant over a number of years.

9. What are the major risks facing the business?

Although this is something most Companies have historically been reluctant to talk about, new ASIC guidelines ensure that all Companies must at least discuss the important risks to their business in their Annual Report. While there is some variation as to the quality of these discussions in Australia, and they do have some way to go to catch up with the detail provided by most US-listed companies, companies such as Rio Tinto is doing an excellent job even separating the risks to the business under the headings ‘External Risks’, ‘Strategic Risks’ and ‘Financial Risks’. Investors need to develop an appreciation of these risks for successful investing.

John Daly, Listcorp

Taxing of Superannuation Pensions

AIA Member

I write in response to the letter from a member published in a recent ‘Member Update’, regarding the tax on superannuation. Some suggest that superannuants should be prepared to pay tax on their pensions, and in so doing, make their contribution to the services and facilities that we all enjoy. A reasonable assertion perhaps.

Some are said to be taking vacations at the tax-payers expense and enjoying the pleasures of river cruising! However, unknown to us, these ‘cruisers’ may have been prudent all of their life - not given to regular excesses, and saving, rather than spending on what they may have regarded as frivolous nonsense. We are all entitled to manage our own saving and our own spending as it suits us. Who are we to judge?

There can be no question that the country requires revenue in order to fund all government services and this revenue comes from taxation in all of its many forms.

However, we must have an informed and rational debate about this taxation, and we must decide as a country, where and how that taxation burden should be spread. We need to decide who contributes what.

Whilst some may view an un-taxed superannuation pension as an unreasonable benefit, others may complain about government funded childcare as equally unreasonable- both may be seen to benefit a small cohort of the population. They are all entitled to their point of view.

One of the most substantial imposts on the government coffers is welfare, including aged pensions. As we are all well aware, the ageing population is progressively exacerbating this problem, to the point where unless some significant action is taken, the cost will soon be unaffordable, if it has not become so already.

Therefore we must act to contain the escalating cost of the aged pension. We must consider ways of encouraging our fellow Australians to save for their own retirement where they are able, and not burden the public purse with a call on the aged pension.

So how do we provide this encouragement? The only possible real encouragement is a financial one. That is, it has to be made attractive to save so as to provide for one’s own retirement and not be a drain on the rest of us. So how is this saving to be made attractive? What can we offer as an incentive? It may be that the only viable incentive is a tax advantage, in whatever form we believe best serves the greater interest.

So the debate needs to be – what is best for the country? Aged pensions for all, or an incentive for those who are able to save to take care of themselves?

An AIA Member



An AIA First! Create your own investment plan

Through a series of modules, attendees will be guided through the process of creating their **personalised investment plan**. Participants in the investment planning workshop will be sent a **workbook before the conference**, so that they can arrive prepared to define their investment goals, needs and strategies through a structured series of interactive presentations.



Full details, and bookings on the AIA Website
www.investors.asn.au

or phone the office on 1300 555 061

Federal Budget Briefing

Sornem Private Wealth, May 2015

Last week the Treasurer handed down the 2015 Federal Budget, with a focus on returning the budget to surplus. We have provided a summary of how these may impact you and your family. With specific focus on:

- ☑ Personal Taxation
- ☑ Superannuation
- ☑ Government & Centrelink Benefits
- ☑ Small business

It is important to note that the Budget announcements are still only proposals at this stage.

Personal Taxation

There were no changes to personal marginal tax rates for residents in this year's Budget. However, the following changes in relation to personal income tax were announced:

Motor vehicle expense deductions

- The number of methods available for calculating tax deductions related to the business use of a motor vehicle will be reduced from four to two, with the '12 per cent of original value method' and 'one-third of actual expenses incurred method' to be removed with effect from the 2015/16 financial year
- The 'cents per kilometre method', which currently provides a deduction based on the size of the motor vehicle's engine, will also be modified. The reference to engine capacity will be removed and a flat rate of 66 cents per kilometre will be applied to determine an individual's deduction amount under this method.

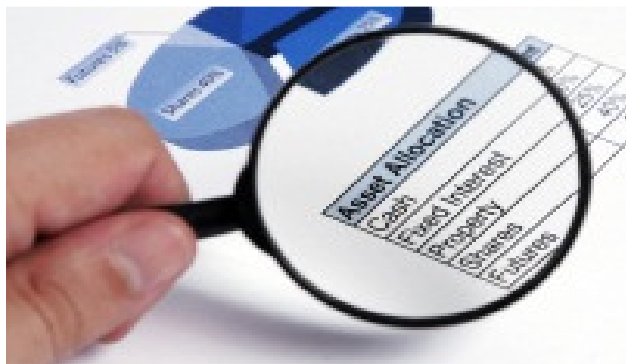
Fringe Benefits Tax (FBT)

- Employees of public benevolent institutions, health promotion charities, public and not-for-profit hospitals and public ambulance services are currently able to salary sacrifice unlimited meal entertainment benefits without being subject to FBT or the benefits being reportable.
- From 1 April 2016, a new separate single grossed-up cap of \$5,000 will apply for salary sacrificed meal entertainment benefits for employees of these institutions. All use of meal entertainment benefits will now be a reportable fringe benefit.
- Meal entertainment benefits exceeding the separate grossed-up cap of \$5,000 can also be counted in calculating whether an employee exceeds their existing FBT exemption or rebate cap.

Employee Share Schemes - further changes to tax treatment

The Government will make further amendments to the proposed changes to taxation of Employee Share Schemes (ESS) from 1 July 2016. The aim is to make ESS more accessible for Australian businesses and their employees, especially start-ups. This measure addresses:

- Providing the CGT discount to ESS interests that are subject to the start-up concession, where options are converted into shares and the resulting shares are sold within 12 months of exercise.
- Allowing the Commissioner of Tax to exercise discretion in relation to the minimum three-year holding period where there are circumstances outside the employee's control that make it impossible for them to meet this criterion. ESS interests provided at a small discount by eligible start-up companies will not be subject to up-front taxation if they are held by the employee for at least three years.



Fly-in fly-out workers ineligible to the Zone Tax Offset

Fly-in fly-out (FIFO) workers whose normal place of residence is outside the remote 'zone' will be ineligible for the Zone Tax Offset (ZTO). Currently, workers whose normal place of residence is outside the 'zone' can benefit from the offset by working in a specified remote area for more than 183 days in an income year.

Higher Education Loan Programme – recovery of repayment from overseas debtors

The Government will extend the Higher Education Loan Programme (HELP) repayment framework to debtors residing overseas for six months or more. People with a HELP debt will be required to make repayments if their worldwide income exceeds the minimum repayment threshold at the same repayment rates as debtors in Australia.

Increasing the Medicare levy low-income thresholds

The Government will increase the Medicare levy low-income thresholds for singles, families and single seniors and pensioners to take into account of movements in the Consumer Price Index. Taxpayers with taxable income below this threshold are exempt from paying Medicare Levy.

Medicare Low Income Thresholds

	Current	Proposed
Individuals	\$20,542	\$20,896
Married Sole Parent	\$34,367	\$35,261
For each dependent child or student, add:	\$3,156	\$3,238

Medicare Low Income Thresholds – people entitled to seniors and pensioner offset

	Current	Proposed
Individuals	\$32,279	\$33,044
Married Sole Parent	\$46,000	\$46,000(1)
For each dependent child or student, add	\$3,156	\$3,238

(1) Assume no change to this threshold as it is not mentioned in the budget papers

Superannuation

Early access to superannuation for people with a terminal illness

The Government intends to amend the superannuation conditions of release to make it easier for people suffering a terminal illness to access their superannuation benefits from 1 July 2015. Under the current rules, a person with a terminal illness can only access their preserved super benefits where they are diagnosed as having less than 12 months to live. The Government plans to amend the relevant regulations to change the life expectancy period to 24 months. This change will provide people with access to their super savings earlier which may assist with the payment of treatment costs and allow them to make the most of time with their family.

Government & Centrelink Benefits

Pension asset test changes

From 1 January 2017, the following changes to the pension asset test have been proposed:

- increase the 'asset free areas' for both homeowners and non-homeowners
- increase the asset test taper from \$1.50pf to \$3pf per \$1,000 of assets over the lower threshold.

According to the government the proposed changes will result in some people either completely losing their age pension entitlement or having their entitlement to a part pension reduced. Conversely, other people may see a small increase to their entitlement. For example, the government has forecasted approximately:

- 91,000 will lose entitlement to the pension
- 235,000 will have their pension reduced
- 170,000 will receive a pension increase.

Asset free area changes

The proposed changes to the asset free area (the lower assets test threshold) are:

- For homeowners – the asset free area is proposed to increase from \$202,000 to \$250,000 for singles and from \$286,500 to \$375,000 for couples. This represents an increase in the lower assets test threshold of \$48,000 and \$88,500 for singles and couples respectively.
- For non-homeowners – the asset free area is increasing from \$348,500 to \$450,000 for singles and from \$433,000 to \$575,000 for couples. This represents an increase in the lower assets test threshold of \$101,500 and \$142,000 for singles and couples respectively.

For those with lower levels of assets, these changes may result in an increased rate of age pension. The government has also confirmed the comparatively larger increase in the lower assets test level for non-homeowners is in recognition of higher living costs.

Asset test taper

The asset test taper rate (the amount by which a person's pension entitlement decreases under the assets test) is proposed to increase from \$1.50pf to \$3pf per \$1,000 of assets over the lower threshold.

Under these proposed changes the asset test taper rate will return to 2007 levels and will result in a substantial reduction in the upper assets test threshold. This table sets out the current and proposed asset test thresholds:

PENSION ASSETS TEST

	Current Lower Threshold	Proposed Lower Threshold	Current Cut-off Limit	Proposed Cut-off Limit
Single Homeowner	\$202,000	\$250,000	\$755,500	\$547,000
Single Non-Homeowner	\$348,500	\$450,000	\$922,000	\$747,000
Couple Homeowner	\$286,500	\$375,000	\$1,151,500	\$823,000
Couple Non-Homeowner	\$433,000	\$575,000	\$1,298,000	\$1,023,000

Concession cards

The government estimates that approximately 12% of pensioners will lose entitlement to the pension as a result of the changes to the asset test. These people will automatically be issued with a Commonwealth Seniors Health Card, or a Health Care Card for those under pension age.

Defined benefits scheme income test treatment

From 1 January 2016, the level of income that can be excluded from the pension income test will be capped at 10%. The Government claims an anomaly was

unintentionally created in 2007 which allowed some people to exclude a large percentage of their defined benefit income stream from the pension income test. The Government states that around 65% of income support recipients with payments from defined benefit schemes have deductible amounts of 10% or less and will not be affected by this measure.

Department of Veterans Affairs pensions and defined benefit pensions paid by military superannuation funds are proposed to be exempt from this measure.

Rental income to be included in aged care means tests

New aged care residents who enter aged care from 1 January 2016 will have their rental income from renting out their former home included in the calculation of their means tested amount. This differs from current rules, where residents who pay some or all of their accommodation payments as periodic payments are entitled to an exemption on the rental income from their former home when calculating their means tested amount for aged care fee purposes. The Government claims this measure aligns the aged care means testing arrangements between those that pay their accommodation payments as lump sums and those that pay periodic payments.

New child care subsidy

From 1 July 2017, a new single Child Care Subsidy (CCS) will be introduced. CCS will replace the existing:

- Child care benefit and
- Child care rebate.

CCS will be payable to families who use an approved child care service for a child who is under 13 years of age. In addition, they need to meet an activity test (working, studying, training or other recognised activity).

Child Care Subsidy payments will be paid directly to approved child care service providers. Families will pay the gap between the level of subsidy they receive and the actual fee charged by the service.

The amount of Child Care Subsidy payable is determined by:

- amount of work, study, training or other recognised activity undertaken
- hourly caps depending on the type of care
- family income

Cessation of the Large Family Supplement of Family Tax Benefit Part A

Currently the Large Family Supplement is paid as part of Family Tax Benefit Part A to families with three or more children. The Government has proposed the following changes:

- From 1 July 2015 to 30 June 2016, the Large Family Supplement will only be paid to families with four or more children.
- From 1 July 2016, the Government will cease to pay the Large Family Supplement.

'No Jab No Pay' policy

From 1 January 2016, families will no longer be eligible for subsidised child care or the Family Tax Benefit Part A end-of-year supplement (up to \$726.35 for each child) unless their child is up-to-date with all childhood immunisations. Exemptions will only apply for medical reasons.

Paid parental leave

The Government will remove the ability for individuals to double dip when applying for the existing Parental Leave Pay (PLP) scheme, from 1 July 2016. Currently, individuals are able to access payments from both the Government PLP scheme in addition to any employer-provided parental leave entitlements. However, the Government has confirmed it will ensure that all primary carers would have access to parental leave payments that are at least equal to the maximum PLP benefit (currently 18 weeks at the national minimum wage).



Small Businesses

The Government announced a range of tax concessions to assist small business entities. Generally, a business is a small business entity if it has business turnover (aggregated turnover) of less than \$2 million.

Company tax cuts

A tax cut of 1.5% is proposed to apply to all incorporated small business entities from the 2015-16 financial year. If implemented, this measure will reduce the company tax rate for small business entities to 28.5%. Importantly, the Government has confirmed the current maximum franking credit rate of 30% will remain

unchanged for all companies, maintaining the existing arrangements for investors, such as self-funded retirees.

Unincorporated small business tax cuts

Individual taxpayers with business income from an unincorporated small business will be eligible for a 5% tax discount on income tax payable on business income received from the 2015-16 financial year. The discount will be capped at \$1,000 per individual for each income year.

Expansion of accelerated depreciation

Small businesses will be able to claim an immediate deduction on assets that cost less than \$20,000 they start to use or install ready for use, between Budget night and 30 June 2017. Assets valued at \$20,000 or more can continue to be placed in the small business simplified depreciation pool and depreciated at 15% in the first income year and 30% each income year thereafter.

The Government will also suspend the current 'lock out' laws for the simplified depreciation rules (these prevent small businesses from re-entering the simplified depreciation regime for five years if they opt out) until 30 June 2017. From 1 July 2017, the thresholds for the immediate depreciation of assets and the value of the pool will revert back to existing arrangements.

Deduction on professional advice fees relating to establishment of a business

New businesses will be able to claim an immediate deduction on a range of professional expenses associated with starting a business, such as professional, legal and accounting advice. This measure is proposed to apply from 2015-16. Expenditures on commencement of a business are currently not eligible for immediate deduction as it's considered an outgoing of a capital nature. Instead, they are currently written off over five years i.e. 'black hole expenditure' under section 40-880 of ITAA 1997. This measure will allow more money to be invested in the growth of new businesses.

Capital gains tax roll-over relief for changes to entity structure

From the 2016-17 financial year the Government proposes to allow small businesses to change legal structure without attracting a capital gains tax (CGT) liability at that point. Currently, CGT roll-over relief is available only for individuals who incorporate but all other entity type changes have the potential to trigger a CGT liability.

Fringe benefit tax change for work-related electronic devices

From 1 April 2016 a fringe benefit tax (FBT) exemption will be available to small businesses that provide employees with more than one qualifying work-related portable electronic device, even where the item has substantially similar functions. This removes confusion in relation to the current rules where an exemption is only provided for one work related portable electronic device of each type.

Accelerated depreciation for primary producers

From 1 July 2016, the Government will allow all primary producers to immediately deduct capital expenditure on fencing and water facilities, as well as allow primary producers to depreciate over three years all capital expenditure on fodder storage assets such as silos and tanks used to store grain and other animal feed.

Apply GST to off-shore suppliers of digital products and services in Australia

The Government has announced GST will apply to off-shore supplies of digital products and services imported by consumers from 1 July 2017. Currently GST doesn't apply to cross border supplies and all revenues raised from this measure will go to the States.

Sornem Private Wealth comment

The 2015-16 budget deficit forecast has been revised up to \$35.1bn, more than double the estimate from 12 months ago, but only marginally less from the \$41.1bn deficit expected for 2014-15. The budget puts forward underwhelming propositions which are likely to not spur on any significant change in the economy. The 2015 Federal Budget appears to have been designed to predominantly encourage activity within small businesses and start-ups. Although there were amendments which will effect a marginal portion of retirees with the proposed tightening on the asset test, it is expected 12% will lose government entitlements. Typically we expect that the proposals will not be passed without amendments, as all sides of politics will have it out over the next few weeks.

This article is included with the kind permission of Sornem Private Wealth.

Bet on the Casinos, Not on the Tables

Jason Sedawie

I'm personally not a big fan of gambling – casinos have an edge over their customers. Even if the casino loses, the winning punter tends to splurge on restaurants and shopping sprees within the casino, giving the casino owners another opportunity to take the money back.

That's why I was interested in looking at Macau's casino stocks, which have halved over the past year. The halving in these stocks was enough of an excuse to go on a plane and have a closer look. I was curious to meet with gaming executives, see whether they gambled, and if so where. They can't gamble at their own casino, but the answer was always 'no'.

Of course they don't gamble – they know the statistics involved! On average, whenever a mass-market gamer drops \$100 on the table they walk away with \$75, leaving the casino with \$25. VIPs are treated better on average, walking away with \$97 after spending \$100.

After meeting with them, I was reminded that it pays to be an owner rather than consumer of a good business.

***Becoming an owner & not a consumer***

As consumers we know a lot about what we buy and why we like it over competing products. We can use this to benefit our portfolios. If people really like the product, we should consider the stock. Some businesses (like casinos) are so profitable that management and staff would rather own the business than use the product.

As consumers we know a lot about what we buy and why we like it over competing products. We can use this to benefit our portfolios.

As for Macau, it is struggling. In February gaming revenues were down by half due to the austerity and anti-corruption campaign in China. High rollers are not taking the risk of being seen gambling. It's not worth drawing attention to themselves, as the risk of a corruption investigation means that they may never be seen again.

Macau's future lies in catering to mass-market consumers, not VIPs. Macau has plans to become like Las Vegas, where it is as much about buffets, shows and conventions as gambling.

The leader in this transformation is Las Vegas Sands (LVS). It is famous for owning theme-based properties such as the Venetian in Macau and Marina Bay Sands in Singapore. The Marina Bay Sands casino is its newest addition; with a beautiful infinity pool on top, it holds a 94.8% occupancy rate at an average daily rate of \$414. Both of these properties give guests unrivalled entertainment, shopping, conventions and even gondola rides. They are aiming for a travel experience rather than the gambling-only properties commonly seen in Macau.

The Vegas strip, Macau style

Las Vegas Sands had the vision to construct the equivalent of the Las Vegas Strip in Macau, calling it the Cotai Strip. It even built the land! Cotai was a land-reclamation project joining two islands together. The reclaimed land is being developed to rival the Las Vegas Strip in entertainment, having already passed it in gambling revenues. Las Vegas Sand properties, including the Venetian, have prime position

Jason Sedawie, Decisive Asset Management

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