

THE FINANCIAL STATEMENT

A NEWSLETTER ON ECONOMIC, ACCOUNTING, INVESTMENT, TAXATION AND BUSINESS NEWS

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FLOOD & CYCLONE DISASTERS

(Time of writing 1st March, 2011)

by Peter Small, B. Bus, F.C.A., Dip. Fin. Services, and
Evan Kambourakis, Dip. A, B. Com, ASA

The devastating floods that hit Queensland, northern New South Wales and Victoria in early 2011 and then Cyclone Yasi which hit northern Queensland on 3rd February, 2011, will provide challenges to the entire nation for years to come. News reports carried chilling images of the destruction to lives and property around the world, but except for the immediate cleanup work, the aftermath of the flooding and cyclone damage is unlikely to attract significant media attention, even domestically.

However the effects are already in evidence. Increases in prices of some foods due to crop losses were almost immediate across the nation, and will continue for some time. These price increases will put upward pressure on inflation and as a consequence, possibly on interest rates as well. Commonwealth Bank economist Mr James McIntyre believes that the Reserve Bank of Australia (RBA) will not raise the current cash rate of 4.75% until later this year.

Costs of labour, construction materials and insurance premiums are also expected to increase nationwide, in some cases substantially. Much of the damage, especially to roads, railways and bridges, are presently being inspected and addressed. Some office buildings, for instance, are expected to be unoccupied for weeks or even months, depending on the extent of any repairs found to be necessary. Damaged domestic properties may remain derelict for extended periods

of time, as resources will be applied to new construction rather than to demolition jobs (this has been the case in New Orleans). It is probable that changes will be made to planning laws in an effort to reduce the chance of a repetition of the effects of another flood event. Some land areas may be declared flood-prone and unable to be built on. Owners of properties in such locations would likely see the value of their holding disappear. Insurability may become an issue for some properties/ businesses in areas that have a flood-history, and premium increases are going to be felt everywhere to help cover the costs of policy payouts.

The effects of the floods and cyclone on government budgets are yet to be determined. The federal government will try to pass a once off 1.8 billion dollar levy through parliament. If successful, the levy along with savings from budget spending cuts will be used to offset part of the costs of rebuilding. However, increasing personal tax rates may not be a viable option, from a political point of view. Nationwide, consumer spending is already fragile, and housing construction has been subdued, with the result that economic growth was only 0.2% before the floods and cyclone hit. As an alternative, the government could, though it is not likely, delay returning its budget to surplus, and in this way borrow to fund reconstruction costs.

If you are interested in the Global Financial Crisis (GFC) OR The World Financial System, DO see the Academy Award winning documentary "Inside Job". Otherwise don't. Also not suitable for children.

The cost to industry sectors is also yet to be calculated. Queensland, for example, produces some 56% of the world's coking coal, but only 15% of mines in the flooded areas are fully operational, with almost 20% completely closed and the rest on reduced production or experiencing difficulties in transporting output (4 mines will have no rail service for at least 3 months). Many of the affected coal mines are the open cut type, and before these can recommence operations they need to be pumped out. Pumping requires environmental impact assessment, and drains yet more water into already flooded river systems. Many other major corporations have revised earnings forecasts downwards, and replacing plant and equipment will for some be a difficult and costly undertaking, further eroding their profits.

In the case of small businesses, both rural and urban, even a short-term interruption to trading can see many unable to sustain themselves until their business returns to normal trading conditions. The Queensland fishing and shellfish industries are also forecasting substantial damage to their catches, as freshwater affects marine areas. Any damage to the Barrier Reef and its surrounding ecosystem that may result from an increased level of freshwater in the ocean may be felt for decades to come. Tourism is a substantial part of the economy in Queensland, which supplies 25% of Australia's tourism accommodation. Even before the floods and cyclone, the sector was suffering due to the high Australian dollar. Cancellations of bookings have occurred, and not only in areas directly affected. On a positive note, there will certainly be an increase in economic activity, as a result of rebuilding (both at a personal and public level). Employment opportunities for those involved in reconstruction will be plentiful, and already tradespeople from outside the flooded areas are moving in to assist in the rebuilding. Even insurance assessors have been brought in from interstate and overseas to increase the speed at which claims can be settled. Households will need new furniture (and in far too many cases, a whole new house), while farmers and other businesses will need to buy new equipment, and government will need to spend money to repair or rebuild infrastructure.

However these resources would, in the absence of the floods and cyclone, have been directed to more productive areas. To give an example, building a house to replace one destroyed is not as economically productive as building a new house, although the replacement assets should be more modern, and therefore more valuable, than the ones

being replaced. In addition, an increase in retail spending (such as for the replacement of lost possessions, vehicles, equipment etc) in turn can contribute to inflationary pressure.

Property prices and leases in areas near, but outside, the flood and cyclone affected areas are in high demand, and will continue to be as reconstruction workers require accommodation. Short term commercial rentals are also highly sought after, to accommodate businesses until their permanent facilities are available once more. Cold storage facilities are also experiencing a major upturn.

The real positive comes from the fact that floodwaters do not just dry up and disappear. Rather, the waters will be carried downstream, affecting other regions, although not so severely. Floods often leave a new layer of topsoil, thus replenishing minerals in the ground. Sub-surface moisture levels and dam levels will be boosted which will assist with irrigation of future crops, both in the affected areas and further downstream. In Queensland, this outcome should benefit wheat growers west of the flooded areas and wool growers further south. As the floodwaters flow south through New South Wales they will make a major contribution to the environmental repair of areas that have been damaged by years of drought and over-irrigation.

Several major lessons should be learnt from the floods and cyclone. Having adequate insurance is a must for everyone, business and individual alike. Maintaining records of valuable assets, including photographs where appropriate, is important in the event of an insurance claim. Disaster recovery plans are essential for every business, enabling operations to recommence quickly, even in a different location.

The enormous direct costs, estimated at between \$16 and \$20 billion, will be met by insurers, the various levels of government, and the private sector. In addition, large donations have been pledged both locally and internationally to provide assistance to victims. Many aspects of the cost, however, are not easily quantified. There are some who will benefit from these disasters, but for the nation as a whole the costs will be substantial.

We are available to give personal advice on taxing issues arising from the recent natural disasters. Special assistance is being given by the state governments of Queensland, Victoria and New South Wales, and by the Federal Government. Do contact Peter Small or Evan Kambourakis.

by Nuha Awad, B. Bus, (Accounting)

Honesty is a fundamental principle in every organisation culture's DNA. Honesty in the workplace will breed better managerial decisions, produce higher productivity and improve employee morale.

To invite honesty into an organisation, there is a need to create a culture of open communication which means that the organisation must be open to discourse and criticism from staff. Employers should encourage employees to express their opinions openly and honestly.

Here are some tips for an honest organisation culture:

1. Employers should encourage employees to avoid saying what the leaders and clients want to hear and stick to clarity and honesty with tact.
2. If employers get angry at employees who bring them bad news, then they will never hear bad news until it is too late. Management may show it values candour and honesty to reduce the likelihood of cover-ups of mistakes and to put measures in place to rectify them quickly.
3. A lack of trust puts customers and staff on guard. By bestowing trust, companies can win the loyalty of their employees and create an innovative working environment.
4. Employers may consider introducing open door policies, ethics training and setting up internal blogs that give a voice to people whatever their position in the business.
5. Employers can educate staff regarding expectations and policies relating to honesty. They can put in place counselling and discipline policies as soon as dishonesty is known and make sure that action is consistent.
6. Admission of mistakes is empowering and encourages staff to do the same. Going public with a failure allows the employers and/or the company to re-establish itself, what it stands for and can disarm critics. Confess, take immediate action and move on.
7. Employers should not allow the idea of honesty or ethical behaviour to be a little isolated zone where good deeds are done, allowing the rest of the organisation to act as it likes. Actions of honesty should be designed to fit with the company's mission and character, and to maximise the impact on the function of the company.

E-SHOPPING

by Evan Kambourakis, Dip. A, B. Com, ASA

Recently, retail stores Myer and Harvey Norman argued a campaign for the Australian Government to impose GST on small valued imports. This argument brought on debate by various people, retailers, consumers, and a response by the Prime Minister of Australia Ms Julia Gillard.

The Prime Minister sided with the majority of consumers stating that E-Shopping offered consumers convenience and opportunities for shoppers purchasing items that were less than \$1,000. Such small items are currently exempt from GST when they are imported. Ms Gillard advised that administration costs to recover GST on overseas goods would be much higher than the GST involved and therefore, not feasible.

This is an opportunity for Australian businesses and consumers to purchase small items at bargain prices from overseas suppliers, given that the Australian Dollar is currently very strong.

E-Shopping represents competition for Australian retailers. This may urge many retailers including Myer and Harvey Norman to offer online trading from overseas, so that consumers obtain the GST benefit. Many retailers may also close retail outlets and join online retailing to save on operational costs, such as wages and rent if the majority of their customers shop online.

Should you be considering purchasing items from overseas, take caution and look for hidden costs (eg credit card foreign transaction fees, credit card currency conversion rates) and overseas warranty cover issues. Also have a review of a checklist on the Australian Competition Consumer Commission (ACCC) website and details at Econsumer.gov to better understand your rights as a consumer when purchasing from overseas.



by Karen Huynh, Adv. Dip. Acctg.

Any form of financing made according to Islamic law forbids the payment or receipt of interest. They are interest free loans. For example: they work by a bank buying an asset, then placing it up for sale to the customer at a profit, then the customer makes repayments in instalments. The bank's profit cannot be clearly defined, there are no additional penalties for late payment. In order to protect itself against default, the bank asks for security.

A key difference of an Islamic loan is when a borrower misses a repayment. With an interest based loan, interest is added to the loan and charged on the higher amount. Through Islamic funding, interest cannot be added, the missed payment is added to the end of the loan.

The charging of larger fees as distinct from interest is another method used by financial institutions.

At the request of the Government on the 13th October, 2010 the Chairman of the Board of Taxation, Mr Dick Warburton AO, announced the release of a discussion paper based on a complete review of Australia's tax laws to make certain that they do not hold back the expansion of Islamic finance, banking and insurance products.

Most Islamic loans are like partnerships or joint ventures, but they are called loans because they achieve the same result as conventional loans.

Many of Australia's financial institutions offer Sharia compliant finance. This is a growing market in Australia.

Please call St Clair partners should you have any questions on (02) 9221 4088.

BRAIN BOOSTING

by Karen Huynh, Adv. Dip. Acctg.

Do you remember the last time you had a big laugh? Did your body feel relaxed? We know that when the mind, body and soul work together, we experience happiness and well-being. It is the brain that helps them work together.

Here are some top tips for brain health:

- Staying in employment – would you believe that work is a key factor in healthy brain bonding?
- Educate yourself – continuation of learning keeps you motivated and it also helps with your imagination.
- Have committed relationships – the ones that you have with your family, friends and colleagues are important.
- Get enough sleep – a lack of sleep affects your ability to make decisions. Going to sleep earlier makes up for lost sleep.

- Cut out technology before bed – it disturbs your sleep which affects your brain and body.
- Do a crossword – it's a fun pastime and resourceful way to keep your brain sharp.
- Volunteer – study shows that doing this has many benefits which includes the development of memory.

It is said that the brain works best when interacting in relationships.

While it is satisfying to quit when you're down, the best thing to do is keep on going.

Remember that by keeping your brain active, it is the best method to keep your brain healthy.



by Peter Small, B. Bus, F.C.A., Dip. Fin. Services

☐ LAND TAX

Owners of land in New South Wales are reminded that Land Tax is assessed on the value of land owned at 31st December each year. Building values are not taken into account. Land owners who will be subject to Land Tax for the first time should contact us to assess their liability and arrange for a return to be lodged. The threshold value for land to become taxable is \$387,000; this value is an aggregate of all land owned in NSW (although an exemption is available for most land owners in respect of their principal residence). The due date for lodgement of returns by first-time payers is 31st March, 2011. Our readers with property holdings in other states should contact us in regard to their exposure to land tax in those states.

☐ SALARY SACRIFICE RULES

The wages authority has confirmed that it is possible for a salary sacrifice arrangement to reduce the salary component to below the minimum wage level, without the arrangement breaching the employers minimum pay obligations. As well as meeting the tax law rules for salary sacrifices, the arrangement must also be in writing, specify the amount of the salary sacrifice deduction, and must be principally for the employees benefit. As an example:

Award Rate (annual)	\$40,000
Total Salary Package	\$45,000
Salary Sacrificed to Superannuation	\$10,000

The result is that the taxable salary in the example is now \$35,000, which is below the minimum award. However, provided the required conditions are met, the employer is not in breach of the award. Any reader wishing to establish a salary sacrifice arrangement should contact us to assess their position before making any decisions.

Amounts salary-sacrificed to make additional employer superannuation contributions are required to be shown on PAYG Summaries, and may reduce entitlements to some benefits for low-income earners.

☐ FRINGE BENEFITS TAX (FBT) - 2011

All employers should remember that the FBT year ends on 31st March, 2011. Any employer who provides fringe benefits to an employee is subject to the FBT rules. Directors of companies are deemed to also be employees for FBT purposes. There is an exemption from FBT for many business tools (including briefcases, calculators, portable computers, mobile phones, and electronic diaries, provided that no more than one is supplied per year for each employee). Minor benefits are also exempt. To qualify for this exemption the benefit must be small in value (\$300 is the maximum) and must not be provided on a regular basis. These exempt benefits are (generally) able to be claimed as tax deductions by the employer, and Input Tax Credits for the cost of the gifts are also available. And finally, gifts, unlike monetary bonuses, are not taxable income to the employees receiving them. Employers should remember these rules when planning staff bonuses.

The value of benefits provided to employees is required to be reported on their PAYG Summary for the year, where the value of the benefit is \$2,000 or more. While we directly contact clients we know to be affected by FBT, we invite other readers to contact us if they require our assistance or believe they may be liable.

Finally, we recommend that loan repayments should be described as such on cheque butts and in cash books, and should preferably be for round amounts, to avoid any suggestion that the payment might be a fringe benefit.

☐ EDUCATION EXPENSE TAX OFFSET

Parents of children going back to school should ensure that they keep receipts for expenditure on school costs, as a claim for a tax offset may be available. Those eligible for the Education Expense Tax Offset will also benefit from an extension to the rules covering qualifying expenditure, scheduled to take effect from 1st July, 2011, which will include the cost of school uniforms.

☐ MEDICAL EXPENSES TAX OFFSET

The threshold for the tax offset for medical expenses is \$2,000 for the 2011 year, so taxpayers who expect to be near the threshold may wish to consider scheduling any expected medical treatment (dental, optical, medical, pharmaceutical, etc) before 30th June, so that the payments will fall into the 2011 year.



by Marc Hurwitz, B. Com, (Accounting)

In the course of running a business there are many strategic decisions that need to be made in order to improve the business and increase the profitability. There are many different techniques that can be used to do this, one of these is a S.W.O.T. analysis.

A S.W.O.T. analysis is a way of evaluating your business and business climate in order to see how best to proceed. S.W.O.T stands for Strengths, Weaknesses, Opportunities and Threats. The Strengths and Weaknesses relate to internal factors of the business while Opportunities and Threats are external to the business. Let's look at them individually:-

Strengths: This refers to what your business does particularly well that would give you an advantage over your competition. This could be the quality of your product, after sales support, pricing and expertise in the relevant field. So once you have identified what your business does particularly well you should look how to expand on them and how to make them more beneficial to your business. This could be by way of advertising that particular aspect of the business.

Weaknesses: These are the parts of the business that leave the business at a disadvantage in

comparison to the competition, which could be advertising, pricing and range of products offered. Once you have identified your weaknesses you can work on converting them into strengths. Which may be done by increasing advertising, altering pricing structure, expanding your range of products and expanding to a new market.

Opportunities: Opportunities are chances in the environment that can be used to expand your business. These can be new products, new markets and change in procedures. Once you have identified the opportunities you go through the process of "matching and converting", which is matching the opportunity with your strength and converting it into one.

Threats: Threats are external factors that have the potential to decrease your market share and sales. This can be a new competitor, new products on the market and weather conditions. Threats have to be prepared for in order to minimise the impact of the threat. So if a new competitor is opening up offering the same goods at a better price you may need to adjust your pricing.

CLIENT AUDIT PROTECTION

by Paul St. Clair, F.C.A., Dip. Fin. Services

Over the last few years Governments and Government agencies have increased their audit activity. The activity arises from BAS reviews, Tax audits, Payroll Tax audits, Workers Compensation reviews, Capital Gains audits, Small/Medium size Superannuation Funds audits, work related expense reviews, Stamp/Excise duty reviews, Building Services Authority audits, Centrelink enquiries, employer obligations and others.

The time and cost involved in these investigations can on occasions cost you thousands of dollars. There are Tax and Government Audit Insurance policies available.

In most cases such premiums are tax deductible. Premiums depend on your category description, e.g. an annual premium would be approximately \$120 for a salary and wage earner; a Self Managed Superannuation Fund \$340; a sole trader with turnover up to \$500k, \$320; a business entity with turnover \$3m to \$6m, \$890 or turnover between \$25m to \$50m, \$3,625.

It may be worthwhile for you at least to consider this form of insurance. Do contact Paul St. Clair on (02) 9221 4088 for further information.



by Paul St. Clair, F.C.A., Dip. Fin. Services

The current MINING boom is the biggest boom Australia has ever had says Michael Knox of RBS Morgans'. Australia has had many mining booms going back to 1870. The first was the gold discoveries of the 1850s establishing Melbourne as the second largest city in the British Empire after London. Not all booms in Australia were mining booms. Australia has had its share of agricultural booms, the most notable being the wool boom at the time of the Korean War. The effect of these booms is to enhance our terms of trade and hence Australia's prosperity. The practical effect is a flow on into other industries such as manufacturing, investment; establishing a larger skilled and unskilled population; transport expansion covering railways, roads, ports and air traffic. So if the current longest boom in Australia's history is managed well this should mean a leap in Australia's prosperity.

SUPERANNUATION is growing and is playing a big role in the Australian economy. In fact it is the largest industry in the Australian economy. Funds under management are now in excess of \$1.4 trillion. Australia has the fourth largest pool of managed funds in the world and is projected to grow to \$5 trillion by 2030. Superannuation investment helped shield Australia from the worst of the Global Financial Crisis (GFC). What followed was a recapitalisation of Australian companies to the tune of \$90 billion in 2008-2009 with much of the money coming from Superannuation. Australia accounted for 10 percent of the world's recapitalisation. All this is possible as a result of compulsory superannuation of 9 percent based on employee's earnings, set to rise to 12 percent by 2020, voluntary contributions by self employed and salary sacrificing. Worthwhile tax concessions support the industry. To find out more do contact Peter Small on (02) 9221 4088.

BAD debts are always a potential problem in credit run businesses. More so after an economic downturn and particularly after the Global Financial Crisis (GFC). A survey undertaken by the Institute of Internal Auditors and credit insurer Atradius shows one in five business suffered a sizeable financial loss as a result of bad debts in the 2010 financial year. Hopefully this is mainly behind us but nevertheless strategies should be in place to minimise bad debts. Obtaining payment up front is the best strategy but not always possible. Obtaining a deposit to cover at least the materials involved may be a partial solution. If the terms for payment are exceeded then pursue the debt for collection in accordance with the firm's strategy for collection. Our experience is that some firms fail in business because they are unwilling to

embark on a strategy for collection. If your business has not got a debt collection strategy or has problems with it do contact Paul St. Clair on (02) 9221 4088 of this office, before it is too late.

US Financial Crisis Inquiry Commission says it was avoidable. Further, the warning signs were ignored; the captains of finance and the public stewards of the financial system had no idea of the risks that were building up in the banking system. The report takes a swipe at the US Federal Reserve for not handling the housing bubble better, when, on occasions, US banks lent on real estate to 'Ninja' people, (no income, no jobs, no assets) as being a sound financial deal! The driving force that kick started the GFC was in one word, 'greed'.

PROPERTY. Comparing house prices in Australia and New Zealand with the USA the values seem worlds apart. Similar properties in Australia may cost \$AUD 4/500,000 and in the USA \$US100,000. What does this mean? It was the property bubble in the USA that brought on the Global Financial Crisis (GFC). In turn the US property market is flooded with properties for sale. In short the market is extremely depressed. On the other hand the Australian residential property market is well priced, with a shortage of properties. Now when the Australian dollar is favourably valued against the US dollar this may give some Australian investors some food for thought. Be very careful as we do not recommend this investment for the average Australian investor, there are many reasons why. Do contact Paul St. Clair if you wish to discuss this form of investment.

GROWTH. The ANZ bank reports that Australia's solid economic performance since 2005 was underpinned by a rapid acceleration in population. The country might have experienced a recession following the Global Financial Crisis if it were not for immigration. Australia's population rose about 467,000 in 2008-09.

LIFE quality. According to the United Nations report on migration, Australia has the second best quality of life in the world. The best was reported to be in Norway. The ranking was made from 182 countries on a scale measuring life expectancy, school enrolments and income. In the same study the US was 13th and Britain 21st. The lowest ranked was Nigeria followed by Afghanistan and Sierra Leone.



- ❖ The February, 2011 national unemployment rate decreased to 5.0%. Inflation for the December, 2010 quarter is currently 2.7% annually. The current account deficit seasonally adjusted, for the December, 2010 quarter was \$7.299 billion.
- ❖ According to the Australian Institute of Company Directors, the number of women appointed to the boards of Australia's top 200 companies increased greatly in the 2010 year, with 24% of appointments being women, compared with only 8% in 2008.
- ❖ The Australian Sports Commission has estimated that 8.2 million Australians, representing 48% of the population aged over 15, are involved in exercise at least 3 times a week. This encouraging result is a significant increase compared with the 37% estimated 10 years ago.
- ❖ The value of the Federal government's guarantee of bank deposits, introduced as a defence measure against the economic crisis, has reached \$1 trillion, and is part of the reason that the government's financial liabilities are now almost equal to Australia's annual economic output of \$1.22 trillion last financial year.
- ❖ A survey by the Australian Institute of Company Directors has concluded that the burden of red-tape and increasing concerns about personal liability are causing people to become reluctant to take up directorships. The study found that more than 700 state and territory laws include provisions imposing personal liability on company directors for breaches of regulations, with New South Wales being named in the survey as creating the greatest number of concerns.
- ❖ Australians continue to provide inadequately for their retirement years, with more than one third expecting to be unable to live comfortably on their superannuation savings after they retire.
- ❖ One in four workers in Australia was born overseas, the highest proportion of any developed nation. As well, Australia has the greatest proportion of foreign born people in the general population. Only the USA and Spain attracted more foreign workers than Australia.
- ❖ The Australian Stock Exchange has reported that the number of transactions handled has increased eightfold over the last 5 years, from 200 trades per minute in 2005 to nearly 1500 per minute in 2010, although the value of each transaction has fallen from around \$38,000 to less than \$9,000. The fall in value is partly a reflection of more small investors entering the market than ever before.

ONE LAST THOUGHT

The greatest obstacle to getting the job finished is getting the job started.

*Help save our environment - please do not throw this newsletter away.
When you have finished with it, give it to a friend!*

