# THE FINANCIAL STATEMENT

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



St. Clair partners JOHN STEWART, MILLER PARTNERS

Chartered Accountants and Business Advisers

Select House Level 15, 109 Pitt St Sydney, GPO Box 1881, SYDNEY NSW 2001

Tel: (02) 9221 4088 Fax: (02) 9221 7498 Email: accountants@stclairco.com.au

www.stclairco.com.au



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## IN THIS ISSUE



# 100 ISSUES

by Paul St. Clair, F.C.A., Peter Small, B. Bus, F.C.A., and Avinash Lakhan, BFA/LLB. C.A

We are proud to provide you with the 100th Edition of our Client Newsletter. Our first newsletter was sent to clients in April, 1981. The newsletter has always been a free service to our clients and to associates.

Looking back at our first issue in 1981 we had some interesting articles for that era. The article "What is Word Processing?" discussed and outlined the advantages of computerised word processing as opposed to using a typewriter. Another article was on how IBM was working on a supercomputer with the potential to have a capacity of a dozen of the largest computers in a space of about the size of a grapefruit. Technology indeed has changed in the last 27 years.

Considerable changes have also occurred in the taxation, accounting and the business landscape. When our first issue was published:

• there were no taxes on capital gains, fringe benefits.

• sales tax applied but was substituted and expanded with the introduction of Goods and Services Tax.

• company income was subject to double taxation, and death duties applied.

• business entertaining was tax deductible, and there were no penalty tax rates on children's investment income.

• interest rates on bank overdrafts were between 12.5% and 15.5%, and 11.35% on home loans.

• pensions were not included as taxable income, and the superannuation system was not subject to tax. inflation was 9.2% and the All Ordinaries Index was below 800 points. (Now some 6485.)

• The Australian dollar was a regulated currency (it was floated in December, 1983).

Our February, 1984 lead article advised clients on the new health system called – Medicare. In May 1985 we argued against the introduction of Capital Gains Tax. In our September, 1987 newsletter we stated the following on the Australian Stock Market – "...Investors… should now be adopting investment strategies appropriate to the mature stage of this investment cycle.." In December, 1987 our lead article was "Responding to the Crash". In June 1992 we advised clients on the compulsory superannuation guarantee charge coming into effect in the 1992-1993 financial year. Interestingly our lead article in June 1992 was "The Recession Has Bottomed"

Our "one last thought" item has some classic quotes. These are some of the top picks:

"Always look ahead – there are no regrets in that direction"

"A smile is a shortest distance between two persons"

"If anyone believes that the world owes him a living, he should go out and collect it"

However our "one last thought" item in our first newsletter remains as applicable today as it was in 1981.

"We, in Australia live in a privileged corner of a poverty stricken world. We have one of the highest living standards in the world and custody of one of the richest countries. To countless millions elsewhere our lot is utopian. Let us be more considerate."

by Peter Small, B. Bus, F.C.A.

The start of the new financial year on 1st July, 2007 introduced major changes to superannuation. It is appropriate to summarise the new rules, and to consider strategies that are appropriate to benefit from them.

## GETTING IN ON SUPERANNUATION

Participation in the superannuation system is encouraged by tax concessions. Employers and the self employed are eligible to claim tax deductions for making contributions to superannuation. A maximum of $50,000 (including salary sacrifice arrangements) can be contributed for a person each year (known as concessional contributions). Between 1st July, 2007 and 30th June, 2012 a transitional concession cap of $100,000 will apply to persons aged 50 years and over. As well, non-concessional contributions of up to $150,000 per person may be made each year (three years worth can be accumulated into one, giving a $450,000 maximum every three years).

Capital gains made on the disposal of businesses are eligible to be rolled over into superannuation, instead of being subject to tax under the Capital Gains Tax (CGT) provisions. This effectively defers CGT until retirement (and may even eliminate the CGT entirely, if the benefit is paid out tax-free, as described below).

Low income earners are further encouraged to make non-concessional contributions, by a Government Co-Contribution. Contributions made by those on low incomes are matched by a Co-Contribution Payment of $1.50 for every $1 contribution, up to a maximum Co-Contribution of $1,500 each year (for eligible contributions made during the 2006 year, a one-off Co-Contribution Bonus of $1.50 has been announced, bringing the total for that year to $3 for every $1 contributed). The Co-Contribution is available for those with incomes up to $58,000 (the full amount is payable on incomes up to $28,000, and then phases out until income reaches $58,000).

The superannuation system is supported further by the Superannuation Guarantee rules, which oblige employers to pay superannuation contributions for most employees, at the rate of 9% of salary for each eligible employee.

## WITHIN THE SUPERANNUATION ENVIRONMENT

Provided the superannuation fund complies with all applicable rules, its earnings are taxed at a rate no higher than 15% (the term income includes concessional contributions). Capital gains made by a superannuation fund are eligible for a one-third discount, so reducing the effective tax rate on gains made by a fund to 10%. As well, income used to make pension payments is tax exempt, so if a fund is only paying pensions, its earnings are tax-free, and this exemption also extends to capital gains.

These tax concessions make superannuation the best structure in which to hold long-term investments.

## GETTING OUT OF SUPERANNUATION

In general terms, money put into the superannuation system must stay there until the person reaches age 55. Withdrawals of benefits by retirees from age 60 are tax-free, whether taken as a lump sum or pension (a rebate applies for retirees aged between 55 and 60). Taking retirement benefits in the form of a pension is generally the better strategy, since the earnings on an invested lump sum would represent taxable income, whereas the pension is not taxable. It is not necessary to retire from the workforce to access superannuation benefits, although benefits taken prior to retirement are not completely tax-free. Previously, the rules required retirees to withdraw their accumulated benefits whether they wanted to or not. These rules have been relaxed, so money can now stay within the superannuation environment indefinitely.

**In our next issue we will look at some strategies designed to take advantage of the new rules.**

by Sunny X Song, B. Pharm, M.Com

As a business person, you are too busy to catch a cold at this time of the year. Why not prepare yourself to beat the winter blues?

Colds are caused by viruses that are easily passed on through sneezing and other contact. With no cure yet developed for the common cold, antibiotics are ineffective against cold and flu viruses. The best prevention for a cold is having overall good health. During the winter months, a good general multivitamin and some extra anti-oxidant protection will help to boost your immune system. The following natural remedies may help to fight against the dreaded lurgy.

<u>Echinacea</u>

Echinacea is the most commonly used herb for colds because of its ability to stimulate natural immunity. It is also antibacterial, antimicrobial, antiseptic and antiviral.

<u>Vitamin C</u>

Despite the huge amount of research, debate still rages over the effects of vitamin C in preventing or treating the common cold. Some researches showed that taking large doses of vitamin C can stimulate the immune system, shorten the duration of cold and reduce the severity of common-cold symptoms.

<u>Lactoferrin</u>

Lactoferrin is an important natural immune compound found in the human body. Particularly high levels are present in colostrums. It is thought to play an important role in the defence mechanisms against bacteria, fungi and viruses by enhancing the immune system.

<u>Garlic</u>

Once garlic is consumed and broken down in the body, its by-products are released through the lungs, where the antimicrobial action helps to kill off any infection.

<u>Zinc</u>

Zinc in the gluconate form needs to be taken when symptoms first appear and then continuously for the duration of the cold. For treating colds, zinc is best taken in the form of lozenges.

<u>Olive leaf</u>

Olive leaf has antibiotic, antibacterial and antiviral properties that make it potentially useful for the treatment of colds.

Overall, a good diet and a healthy lifestyle keeps you away from cold and flu in winter:

- ☑ Drink lots of fluids to keep mucus secretions thin and prevent dehydration.
- ☑ Avoid mucus-forming foods such a dairy products.
- ☑ Avoid central heating because it dries out nasal mucosa – an important defence against invading viruses.

## GO FOR RESEARCH & DEVELOPMENT GRANTS

If your company has an R & D project where you can fund half the R & D cost, and show proven business success, you may be eligible for funding through AusIndustry R & D grants. Assistance worth nearly $2 billion is made available to 9,000 businesses every year through its grants, loans, venture capital support, and tax and duty concessions.

For further information contact Avi Lakhan on (02) 9221 4088.

# CARBON TRADING

by Avinash Lakhan, BFA/LLB. C.A

**What is Carbon Trading?**

Carbon Trading is a scheme whereby an environmental regulator firstly determines total acceptable emissions that a company or group can emit and then divides this total into tradeable units ready for trading.

**How does it work?**

Participants that emit pollutants must obtain sufficient tradeable units to compensate for their emissions. Companies or groups whose emissions are below their given 'cap' will have surplus units which then may be sold or 'banked' for future usage. Companies or groups that pollute beyond their allowances must buy credits or face penalties. This transfer is referred to as a trade. The scheme basically rewards companies and groups for having reduced emission of pollutants.

**What is the intention of Carbon Trading Scheme?**

In a recent paper to the Government the 'Task Group on Emissions Trading' reported that:-

"The increasing weight of scientific evidence indicates that there is significant and damaging growth in the level of greenhouse gases arising from human activity. This will have a detrimental effect on the global environment and generate economic costs arising from adverse impacts on infrastructure and a range of industries, negative impacts on human amenity and degradation of ecosystems…. there is growing acknowledgment that governments, individually and collectively, should act to mitigate the emission of greenhouse gases. The warning signs cannot be ignored."

A Carbon Trading Scheme basically is an indirect form of tax that is payable by companies and groups for emitting carbon dioxide and other greenhouse gases in the environment. The overall intention of the scheme is to reduce the emissions of greenhouse gases into the environment.

# SMOKING BAN

by Marc Hurwitz, B. Com, (Accounting)

In October, 2004, the then NSW premier Bob Carr announced that smoking in indoor areas of licensed premises would be phased out by July, 2007. This plan has been implemented in 4 phases; on 3rd January, 2005, 4th July, 2005, 3rd July, 2006 and finally on 2nd July, 2007.

As of 2nd July, 2007 the following law comes into place, "All enclosed areas of hotels, clubs and nightclubs that are open to the general public must be completely non-smoking, and all areas of Star City Casino with the exception of the private gaming rooms must also be non-smoking". The Star City Casino exception is the only one to the law.

The laws came into place as at 2nd July, 2007 and all hotels, clubs and nightclubs must:-

- Display non-smoking signs in prominent positions in all smoke-free areas.
- Remove from smoke-free areas all ashtrays.

The new regulations are not expected to negatively affect businesses. This is due to the fact that as smokers may no longer frequent the venues, non-smokers will be happier to do so.

## ❑ TAX RATES - 2007

A reminder that the personal income tax rates for the year ending 30th June, 2007 are:-

| Current tax thresholds to 30/6/07 Income range ($) | Tax rate % | New tax thresholds from 1/7/07 Income range ($) | Tax rate % |
|---|---|---|---|
| 0 – 6,000 | 0 | 0 – 6,000 | 0 |
| 6,001 – 25,000 | 15 | 6,001 – 30,000 | 15 |
| 25,001 – 75,000 | 30 | 30,001 – 75,000 | 30 |
| 75,001 – 150,000 | 40 | 75,001 – 150,000 | 40 |
| 150,001 + | 45 | 150,001 + | 45 |

The income tax rate for companies remains unchanged at a flat 30%.

## ❑ LOAN REPAYMENTS SUBJECT TO TAX

A recent Court decision has major implications for those who operate their business in a corporate structure. The Court decided, surprisingly, that repayments by the business of loans made to it by its owners constituted taxable fringe benefits. While this decision may be, and hopefully will be, overturned on appeal, taxpayers who are employees of their business are warned to take steps to avoid demonstrating the critical factors that led to the Court's finding. In short, these factors were: no salaries were paid by the business to the owners, the business yielded only small profits, and the repayments covered the regular expenses of the owners. Accordingly, the Court decided that the loan repayments were, in fact, fringe benefits that were made in place of salaries to the owners as a reward for their employment in the business.

We therefore suggest that all owners who work in the business should be paid a reasonable salary for their work. Salary payments should be made on a regular basis, the same as for other employees with tax withheld. Payments should **not** be made by the employer for the owners private expenses. These should be paid from the owner's personal bank account. Repayments of the loan account, when required, should show the characteristics of loan transactions: the owner should make a written request to the employer for repayment of a portion of the loan, the repayment requested should be a lump sum, and the entry in the accounting records of the business should describe the payment as "repayment of loan".

## ❑ MOTOR VEHICLE EXPENSE CLAIMS

The new rates for motor vehicle expenses using the cents per kilometre method for the 2006/2007 year are:

| Engine capacity (cc) # | Rate per Kilometre (cents) |
|---|---|
| 0 - 1,600 | 58 cents |
| 1,601 - 2,600 | 69 cents |
| 2,601 + | 70 cents |

\# Conventional engines only; half these rates for rotary engines.

## ❑ REMINDERS FOR EMPLOYERS

Employers are reminded that the rate of superannuation contributions required to comply with the Superannuation Guarantee Charge (SGC) laws is 9%, and that contributions must be made every quarter to comply with the rules. As well, employees must be notified, within 28 days of the last contribution each quarter, of the amount contributed for their benefit. There are very few exemptions from SGC (the most common is for those who earn less than $450 in a month), and substantial penalties apply to breaches. Superannuation contributions are only tax deductible when paid. <u>If you fail to make the mandatory contributions, you are liable to pay the SGC, for which no tax deduction is available.</u>

Pay As You Go (PAYG) Payment Summaries must be issued to employees by 14th July, 2007. The originals of these summaries, and the necessary reconciliation statement, must be forwarded to the Tax Office by 14th August. Details of fringe benefits provided must be disclosed on employee PAYG Summaries issued for the 2007 year.

Whilst gathering your tax information for preparation by us, you may like to check the undermentioned items to see if you have included them in your summary of information. Although the following list is not exhaustive, it will serve as a useful guide.

- ***ASSESSABLE INCOME***

**P**AYG Payment Summaries
**I**nterest and royalties
**B**usiness/Partnership – income and expenses
**C**ommissions received
**T**rust income
**A**llowances, benefits, earnings, tips and directors' fees
**D**ividends, including imputation details
**S**hare transactions (full details)
**R**ent received
**S**ale of any asset where the asset was acquired after 19th September, 1985
**T**ermination payments received (with accompanying documents)
**S**ocial Security benefits received
**P**ension/Annuity payments

- ***ALLOWABLE DEDUCTIONS***

**A**dvertising
**B**ad debts (written off during the year)
**B**ank charges applicable to earning income
**B**usiness Expenses
**C**ommissions paid
**C**onvention/Seminar expenses
**C**ontributions to approved superannuation, provident or retirement funds (generally non-employees)
**D**onations & gifts over $2.00 (approved)
**E**ducation expenses - for income producing Purposes
**F**ilm investments
**H**ome office expenses
**T**elephone expenses applicable to the earning of assessable income
**T**ravelling expenses (including overseas with details)
**I**nsurance premiums (business)
**I**nterest on borrowings for business Purposes
**L**easing costs
**L**egal expenses (in certain cases - full details)
**L**osses of previous years in certain cases.
**M**otor vehicle expenses (including business use proportion and log book if applicable)
**N**ewspapers essential to your business
**P**lant, furniture, fittings, motor vehicles etc., subject to depreciation (limited to $57,009 for a vehicle purchased during the 2007 year)
**S**tationery, postage, printing costs
**S**uperannuation contributions
**S**ubscriptions to trade, business or professional associations
**S**un protection, where exposure is a risk.
**P**urchases for resale
**R**ates and taxes on income producing property
**R**epairs to income producing property (not alterations, additions or improvements)
**T**ools of trade
**T**ax agent fees, accounting and audit fees
**W**ages and salaries

These claims are subject to the substantiation provisions, where applicable.

- ***REBATES***

**S**pouse and dependants (subject to any amount of Parenting Allowance received)
**S**ole Parent
**N**et Medical expenses over $1,500 in total (Tax offset of 20% available)
**F**ranked dividends

- ***OTHER***

**F**amily Tax Benefit - names and dates of birth for dependant children under the age of 21 (25 if in full time education). Details of Family Tax Payments received from Centrelink. Spouse's taxable income and childrens income and education status if over 15 years of age.
**T**rade debtors (at 30th June, 2007)
**P**rivate Health Insurance - rebate and surcharge details required, as well as Fund membership number
Stock value at 30th June, 2007 (valued at cost or market replacement value)

**T**rade creditors (at 30th June, 2007, listed under suitable headings) by Paul St. Clair, FCA

**AUSTRALIAN economy.** The latest economic data doesn't get much better. In the first three months of this year the economy grew at 3.8 percent on an annual basis, the fastest in three years. At the same time inflation actually eased. The unemployment rate dipped yet again to a 32 year low of 4.2 percent. Despite a tight labour market the cost of labour actually fell in real terms by 1.4 percent. In March, 2007, 40,000 new jobs were created. As a result of inflationary pressures easing, again interest rates did not rise. Part of the answer to this great news is that immigration is growing at the fastest rate in 17 years and in this coming year growing even faster. Employers and Government seeing the need for skilled employees have targeted migrants adjusting visa requirements. There is a good balance in these numbers. If the supply of workers keeps up with the demand of employers, then inflation is kept in check.

**TAX hit list.** The Taxation Office has advised of the following occupation hit list for the 2007 tax year – motor mechanics, electricians, hospitality workers, mining workers, factory hands, store workers, IT professionals, accountants and high wealth individuals. The Taxation Office would pay special attention to the explosion in work-related expense claims. The average work-related expense claim was more than $2,000.

**ECONOMIC cycle.** A common question on the minds of investors is "has the economic cycle peaked for the sharemarket and will it now favour the property market?" The sharemarket has certainly been breaking records and at the time of writing, shares are down. There are pointers indicating that the share cycle has still not peaked. Whilst the market has risen over 10 percent this year it is still well supported by strong company earnings. Share yields are about 3.6 percent compared with property at about 2.8 percent in Sydney. The overall price earnings ratio of the sharemarket is around 18; a high but not excessive multiple. The current downturn in the sharemarket is a natural consequence after a big run. In general share prices are still reasonable. On the property side of the economic cycle that market has seen poor returns over the last four years particularly in NSW. This may be about to change since vacancy rates on rental properties have fallen from 4.5 percent to 1.3 percent in NSW. This is a strong indicator but with a possibility of a rise in interest rates this casts a shadow over a residential property pick up. We may well be moving closer to an economic cycle change in the share/property markets but not just yet.

**WORKPLACE information.** From 20th July, 2007 every employer in the federal workplace relations system <u>must</u> provide a copy of the "Workplace Relations Fact Sheet" to all their existing employees within three months and to new employees within seven days. This requirement applies to all corporations who are employers and those employers who are covered by a federal award or instrument. If this applies to you and you want copies of the "Workplace Relations Fact Sheet" do contact Karen Huynh on (02) 9221 4088.

**AUSSIE dollar.** Where is it going and what are the effects? At time of writing the Aussie is heading towards US90 cents. On the basis of information available and on the opinion of most experts on this subject the Aussie is heading upwards against the US dollar. From the Australian view point in a boom economy, depending on inflation numbers, there is upward pressure on interest rates which puts upward pressure on the Aussie. Being in the midst of a minerals boom further upward pressure is on the Aussie dollar. If we go back to the last minerals boom the Aussie dollar well exceeded its present value against the US dollar. In brief our interest rates and minerals boom is sucking in foreign capital. On the other hand the US dollar is weaker as a result of its big budget and trade deficits. There are winners and losers with a rising Aussie dollar. Exports are dearer and imports are cheaper. Cheaper imports may save us from an interest rate rise this year. Not all exporters are hurting with a rising Aussie dollar. Those that make their sales in US dollars are not hurting, for example BHP Billiton and Rio Tinto operate in US dollars. It could be said that despite the weakness in the US dollar it is still a de facto "gold standard".

**GOLDEN rules** applied by Christine Manfield of Modern Food Pty Ltd, to good living and business:-

1. Life's too short to eat bad food.
2. Be inspired by what you do.
3. Stay true to your dreams.
4. Don't give in to mediocrity.
5. Don't ever be scared of jumping into the unknown.

Finally, "It's nice to have money, because it gives you the freedom to make choices, and that's where (on occasions) happiness comes from."

- The national unemployment rate for June, 2007 is 4.3%. The inflation rate for the year to June, 2007 is 2.1%, whilst the balance on current account is a deficit of $15.561 billion.
- Sydney now ranks as the world's 21st most expensive city in which to live, with Moscow in first place followed by London and Seoul. In terms of cost of housing affordability, Sydney now ranks as the world's 7th most expensive city, behind Los Angeles at the top of the list.
- Australia's superannuation nest-egg increased by 19.2% in the 12 months to December 31, 2006, and has now passed the $1 trillion (that is $1,000 billion) mark. Australia now has the fourth largest pool of superannuation savings in the world, behind the US, Luxembourg and France.
- The second five-yearly Intergenerational Report has found an easing in Australia's ageing population, resulting from an increase in the birth rate and increases in skilled migration.
- Researchers studying housing affordability have concluded that the rate of population increase is double the rate of housing construction, resulting in continued pressure on housing prices and rents.
- A decision by the High Court has found that an investor who bought shares in a company was entitled to damages for being "misled" by the company, because he bought the shares at a time when the company failed to disclose its dubious financial position.
- In supermarkets, the more a product jumps out at you the more expensive it is likely to be.
- A social survey has revealed that working long hours does not destroy marriages but where a husband works part-time marriage failure is nearly twice as likely.
- According to a new report, the rate of payment fraud in Australia is low by world standards, but we have topped the world for the number of cars stolen each year on a per capita basis. And even on a total basis, we rank number 8 in the world.
- An American study has forecast that Western asset values could halve in the short to medium term as a result of ageing populations, with baby-boomers starting to realise their assets to fund retirement lifestyles. This could, in turn, put downward pressure on real estate and share prices.
- Australians paid an average of $11,976 in taxes to the Commonwealth in 2006, a rise of 5.6% on the previous year. When State and local taxes are added in, the total paid to government in 2006 reached $14,551 per person.
- The world has more billionaires then ever before, and they are getting younger. Forbes magazine lists 946 billionaires in 2007 (793 last year) with an average age of 62 (64 last year). Bill Gates tops the list ahead of Warren Buffett. Russians and Indians made up the greatest number of additions to the list.

## ONE LAST THOUGHT

**When the Tax Office make a mistake, they call it an error.**
**When a taxpayer makes a mistake, they call it negligence**

St. Clair partners

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