



# The Square Orange

#24 April 2007

## Asset Adequacy - Do you have enough?

At OTS Management we are constantly looking for new ways to serve the client better, so having found an impressive software package to perform Asset Adequacy Analysis we immediately leased it to use in our company.

The software is called True North and is used to collate information about your assets and liabilities and simulate long term returns to see if your assets will be adequate for your retirement objectives.

Traditionally people have used straight line averages to predict your future wealth. Unfortunately straight line returns where the market returns the same average increase year by year, has never occurred.



*Your future - enough for your lifestyle?*

Instead of using straight line averages, True North uses "Monte Carlo analysis" which is used in nuclear physics as a probability tool. Decades of historical market data of different asset classes, encompassing different and unpredictable world cycles such as war and market responses, are used to run 300 simulations on your data in order to arrive at a probability analysis of your being able to achieve

your objectives.

According to Geoffrey Harris of Plan B (the licensors of the software), "we are yet to encounter a client who has not expressed genuine appreciation and value in the output of True North."

True North provides a clear and understandable graphic report on the probability of achieving your financial and lifestyle goals. The beauty of the system is that it allows you to determine acceptable versus unacceptable lifestyle trade-offs and alternative investment histories.

Contact us to perform a free "snapshot" of your asset adequacy or a quote on an in-depth analysis.

### Inside this issue:

Small Business Tax	2
St George shares	2
Penalties - Tax Invoices	2
CGT Planning	3
Work related tax deductions	3

### Special points of interest:

- ♦ On this page we outline the launch of a new service - True North Asset Adequacy Analysis. This new service will show you the probability of achieving your lifestyle goals, and the "tweaking" to increase the probability
- ♦ Do you have shares in St George Bank? There may be tax payable on sell-back rights from 2001 (see page 2)

## Family Trust & Interposed Entity Elections - extended time to make these elections

Under the trust loss rules, a taxpayer is subject to concessional treatment, making it easier to claim prior year losses, if they have made a Family Trust Election (FTE) or an Interposed Entity Election (IEE). Also and importantly, elections may be necessary to preserve franking credits flowing through

the trusts.

Due to the complexity of these rules and the potentially adverse consequences of failing to make the required elections, the Tax Office has allowed an extension to make retrospective elections as part of the 2004 income tax returns.

The Commissioner re-

cently announced a further extension of time to make a one-off lodgement of an election up until 31 May 2007. This will allow taxpayers to retrospectively submit their FTEs and IEEs for 2004 and earlier income years. The procedures for lodging these extensions have been posted on the ATO website.

## Proposed Changes to Small Business Tax

In an attempt to standardise the eligibility criteria for small business tax concessions, the government recently released the Exposure Draft Tax Laws Amendment (Small Business) Bill 2007.

The current regulations require small business to undertake separate eligibility tests for tax



*Good news about tax simplification*

concessions relating to CGT, GST, PAYG and FBT. The proposed Bill aims to simplify the system by defining a small business entity as one which has turnover of less than \$2 million. Eligible entities would have access to the following concessions:

- simplified trading stock rules;
- simplified depreciation rules;
- amended assessment period limited to two years;
- immediate deductions for expenses which were previously required to be deducted on a pro-rata basis; and
- accounting for GST on a cash basis, enabling taxpayers to claim input tax credits when they actually pay for acquisitions.

## Tax on St George Bank shares

Overturning an earlier decision of the Full Federal Court, the High Court has found that the proceeds from the sale of sell-back rights granted by St George Bank were assessable as ordinary income.

In February 2001, St George Bank granted sell-back rights to its shareholders as part of an off-market share buyback. The sell-back right entitled the shareholder to sell back one of their shares to St George at a fixed price above the current market value of the shares.

The mechanics of the arrangement

resulted in the taxpayer receiving and then disposing of her sell-back rights.

**Over 80,000 taxpayers affected and Tax Office will be contacting them**

The High Court held (in a 4:1 majority decision) that whether a receipt is income depends upon its nature in the recipient's hands and

not the nature of the expenditure incurred by the other party.

The Court said that while the rights acquired by the taxpayer were a product of her shareholding, they were 'severed' from that shareholding, and accordingly, the market value of the sell-back rights was held to be ordinary income.

The Tax Office has identified that this case affects over 80,000 taxpayers and it will be contacting them to provide advice on the decision and what it means for them.

## Penalties for not issuing GST Tax Invoices

The Tax Office has recently released Practice Statement Law Administration PS LA 2007/3, which relates to the remission of penalties. The practice statement specifically covers:

- the failure to issue a tax invoice or adjustment note as required by the GST legislation; and
- an entity and its agent both issuing separate tax invoices or separate adjustment notes con-

trary to the requirements of the GST legislation.

The practice statement is useful in providing guidance to small and medium sized businesses or partnerships with limited systems for the generation of tax invoices and adjustment notes.

The Tax Office believes the Tax Invoice is integral to the GST system and imposes penalties on businesses

not issuing Tax Invoices. This practice statement gives guidelines as to when penalties can be remitted (withdrawn) in limited circumstances.

The practice statement only deals with the administrative penalty regime and does not cover the remission of the general interest charge (GIC).

# Capital Gains Tax Opportunity? - Forward Purchase Agreements

In a recent decision in *Lend Lease Custodian Pty Limited v. Deputy Commissioner of Taxation* [2006] FCA 1790, the Federal Court overturned an earlier decision of the Administrative Appeals Tribunal (AAT), finding that a scheme of arrangement involving the issue of a forward purchase agreement for the sale of shares did not give rise to a capital gain in the hands of the taxpayer.

The taxpayer, Lend Lease Custodian Pty Limited (Custodian), purchased 172 million fully-paid Westpac Bank (Westpac) ordinary shares at \$3.53 per share in May 1993. In mid-1995, Custodian discussed exiting a large portion of this shareholding with Westpac.

To this end, Custodian entered into an arrangement in 1996 to sell down its shareholding by way of a forward purchase agreement (FPA). An FPA allows an entity to lock in a price for sale or purchase today, although the transaction may be completed at a future date.

The facts of the actual arrangement are complex. Custodian locked in the sale price in 1996, although the sale of the shares would not be completed until January 2000. In doing so, Custodian would guarantee it could lock in a sale price and also, as part of the arrangement, retain its entitlement to receive fully franked dividends for the next four years.

In the first instance, Custodian granted a warrant over \$100 million worth of shares in a public book-build (an invitation to participate in a competitive tender for shares). This measure effectively ensured the arm's length nature of the transaction between Custodian and County Natwest (County), which was intending to buy the \$100 million worth of shares on offer. The

scheme further allowed Custodian to remain beneficial owner of the shares until completion of the contract in January 2000, including rights to vote and rights to any dividends attached to the shares.

**Under what circumstances can a contractual right be considered "property other than money" for capital gains tax purposes?**

The Commissioner did not accept that the consideration for the shares could simply be the amount set by the FPA, and sought to assess Custodian on an amount of additional 'non-cash consideration' — for example, the additional proceeds received by way of the right to retain beneficial ownership of the shares over four years. The Commissioner contended that the taxpayer received something more than cash and that the contractual rights created as part of the transaction carried an inherent value, which was of additional consideration.

The Commissioner determined a value for the rights by calculating the net present value of the dividends over the four years to completion. In order to determine Custodian's capital gain, the Commissioner compared its cost base for the shares to the amount payable under the FPA plus the value of the rights to retain beneficial ownership.

Custodian argued that there was no amount of additional consideration received pursuant to the FPA as a result of the rights. It argued that for the contractual benefit to be deemed to be property, it would need to be property which Custodian had received or was entitled to receive, which was not the case. In

particular, the rights over the shares were already held by Custodian and remained its legal property until completion of the agreement in January 2000. Therefore, no new or additional rights were created or transferred.

The Court agreed with the taxpayer and held that the Commissioner's contention that the rights represented 'property other than money' was incorrect. It follows that the additional capital gain that the Tax Office sought to assess was invalid.

In addition, the Court held that dividends receivable by Custodian were fully rebateable. The Commissioner's alternative argument that the payment of the dividend was the disposition of a right and should be assessed as a gain was rejected by the Court, which found no evidence to suggest that this was the correct view.

The Tax Office has appealed to the Full Federal Court.

## Claims for work-related deductions knocked back

The Tax Office has sent out 226,000 letters to taxpayers in respect of incorrect claims for work-related expenses including self education expense claims where there was an insufficient connection between the work activity and the education expense; car expenses using the cents per kilometre method not supportable by diary or other entries; incorrectly claiming the entire amount of an asset purchase rather than calculating the asset's decline in value; and incorrect calculations regarding the taxpayer's home office expenses.



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*OTS Management is a quality and value driven boutique consulting and accounting company that provides organisational development services to commercial, growth-oriented Small and Medium Enterprises who require business services, advice and coaching.*

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## The Juice

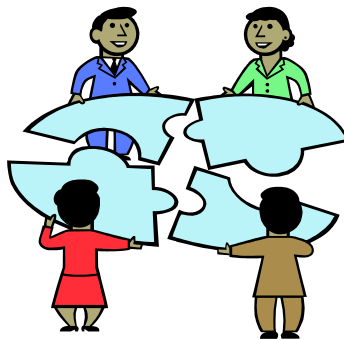
Are you selling a product or a service?

If you are a Qantas Frequent Flyer member, you can avoid the queues and check in at a terminal where, on inserting your card your seat and meal preferences will be known and catered for.

If you subscribe to a major Internet Service Provider today you will be given a free broadband modem.

When you buy a plane ticket, when you subscribe to an ISP - are these products or services?

In today's inter-connected world the best businesses merge their offerings so that products have



**Product or service? It's all in the connections**

services attached and services give you products. If you do not embrace the model where there is no product without service and no service without product, you will be left behind.

For example, say you supply and fit electrical fittings. When you have finished, you usually clean up the room.

Since you have the vacuum out why not clean up the house for free? If in another example you are a lawyer incorporating a company for a client - why not give them a book about running companies?

Your product/service offering today must encompass accessibility, connectivity and intangible or

emotional benefits.

Ask yourself:

- Is your product/service accessible whether in extended office hours, e-mail or helpline?
- Is your product/service available on the web or is it connected to be exchanged or upgraded for another offer?
- Do your customers obtain intangible benefits such as the ability to learn from its use or feelings of security?

Examine your business model to see how it can be adapted to give away allied products or services that can meet the greater demands of today's customers.