

FLOAT  
WATCH

## Tech player at an early stage

### Hazer Group

ASX CODE: HZR  
SHARES ON OFFER: 25 million  
LISTING PRICE: 20c  
MARKET  
CAPITALISATION: \$12.2 million  
LISTING DATE: December 4

SIMON HERRMANN

While initial public offers continue to boom in 2015 it remains a challenge for investors to pick those that offer a favourable outlook.

Hazer Group Limited aims to raise just \$5 million and intends to list on the ASX on December 4. In its prospectus Hazer Group recognises that it is an early-stage company and the success of its business model is highly dependent on technical success of its intellectual property as well as future funding.

As an early-stage company without any significant revenue streams, how promising is the listing for IPO participants?

Hazer Group focuses on advanced materials and is working towards commercialisation of its so-called "Hazer Process". It has intellectual property rights to this technology, which was developed at the University of Western Australia.

The process allows the production of hydrogen gas from methane with negligible carbon dioxide emissions. The difference to other production techniques is the co-production of high-purity graphite. The company has currently three pending patent applications.

The majority of the proceeds raised from the initial public offering will be used to scale up and commercialise the "Hazer Process". Management aims to create shareholder value by developing laboratory equipment and creating a pilot plant that demonstrates the process.

Hazer's management team has a fair track record in the industry as board members were previously involved in the development of technologies and capital market funding on the ASX.

The technology has not reached sufficient scale to generate revenue or earning and will most likely not be able to do so in the next 12 months.

It is not uncommon for companies to list at a pre-revenue stage but the market needs to see evidence that the company is "moving forward" to drive the share price higher. Investors who have participated in the raising will hope for technical breakthroughs, the establishment of partnerships and interest of the general public. However, Hazer is reliant on external funding.

In the absence of revenue and with the technology at a very early stage of the cycle, the initial public offer is lacking catalysts.

Simon Herrmann is an equity analyst at wise-owl.com.

Investors are turning to this area as it grows and matures

ADRIAN HARRINGTON

Investors are increasingly turning their attention to the real estate social infrastructure sector — that is, investments reflecting broader trends in society that, in turn, influence the types of buildings and infrastructure we need as a nation.

Real estate social infrastructure includes investments in the infrastructure behind childcare, seniors housing (manufactured housing, retirement villages and aged care), student accommodation, government premises (police stations, courthouses), and medical and health facilities.

Growth in real estate social infrastructure opportunities is primarily being driven by five factors. • **Demographic and social changes.** Our ageing population is increasing demand for seniors housing and health services, while higher participation of females in the workforce and the growing number of 0- to five-year-olds is increasing demand for childcare. The rise of international students is also one reason the student accommodation market is booming.

• **Demand for better quality facilities.** Operators (tenants) and their customers require higher quality facilities. For example, the childcare sector is moving from "child minding" to early learning, which is changing the design and layout of centres, as they move away from being what were often just converted houses. The healthcare sector is being driven by advances in medical technology and procedures while the aged care sector — supported by government regulation on quality standards — is increasing demand for higher-quality aged care facilities. • **Government financing and budget constraints.** The public



JOHN GOLLINGS

An increase in international students is one of the demographic changes driving the boom in student accommodation

sector's ability to fund the level of infrastructure required to meet the needs of the community is under pressure and governments are increasingly seeking private sector participation.

• **Relatively high population growth rates and greater density and urbanisation of cities.** These factors are increasing the need for investment in social infrastructure assets that support communities both in the inner city and on the urban fringes.

• **Growing realisation operators should focus on their core business.** This means managing and delivering services to the community rather than the provision, ownership and management of the underlying real estate assets.

Of course the benefits of social

infrastructure assets need to be considered in light of the risks.

The key risk to investors is the specialised nature — and often the critical importance — of the operator leasing the asset.

A private hospital is a highly specialised asset and having a well capitalised and competent hospital operator such as Ramsay Health Care is critical.

Successful investing in this

sector requires a sound relationship between the operator (sometimes a government agency) and the real estate owner, and an understanding of the underlying businesses operating within the

facility. Also, social infrastructure assets to varying degrees have high levels of government regulation and intervention that are susceptible to change.

But this can also be a positive, especially if the government is partially or fully underwriting the cashflows of the sector.

While the increased operating leverage and other industry risks clearly warrant a risk premium, the sector's risk-reward profile has improved greatly as many areas of the social infrastructure sector have grown and matured.

Consolidation of operators in the early learning, health and aged care sectors is well under way. Many operators are publicly listed companies. For example, G8 in the early learning sector, Ramsay Health Care and Primary Health Care in the healthcare sector and Japarra, Regis and Estia in the aged care space.

Allowing for these risk factors, investors are increasingly examining real estate social infrastructure as it offers some of the most sought after factors in the present low growth and low interest rate environment.

Perhaps the outstanding attraction is relatively high yields. Social infrastructure asset yields are typically between 100 and 150 basis points higher than major office, retail and industrial assets.

There are also strong real estate factors such as attractive lease structures, "stickiness" of tenants — tenants are inherently linked to their premises due, in many cases, to the specialised nature of the assets — strong demand and government support.

At present, there are five sector specialist A-REITs and four sector specialist real estate developers and managers listed on the ASX, providing exposure to early learning, manufactured housing, retirement, aged care and health/medical.

It is early days, as these entities represent less than 0.5 per cent of the entire listed A-REIT and real

estate manager/developer sectors. By comparison, social infrastructure real estate represents more than 20 per cent of the market capitalisation of the US REIT index.

The performance of the social real estate focused A-REITs has generally been positive. The two best-performing A-REITs in the S&P/ASX 300 Index over the three years to October 31 were both real estate-related social infrastructure A-REITs: Folkestone Education Trust (early learning) and Ingenia (seniors living), with annual total returns of 30.8 per cent and 24.7 per cent respectively, outperforming the S & P/ASX 300 A-REIT Index's 16 per cent.

The unlisted market is also embracing the real estate social

Perhaps the outstanding attraction of the sector to investors is the relatively high yields

infrastructure sector.

Three notable unlisted social infrastructure funds are the Australian Unity Healthcare Fund, which owns more than \$760m of hospitals, medical clinics, nursing homes, day surgeries, consulting rooms, rehabilitation units, radiology and pathology centres; the Folkestone-managed CIB Fund, which owns a portfolio of police stations and courthouses leased back to the Victorian government; and the Transfield-managed Campus Living Villages Fund, which owns a portfolio of student accommodation facilities in Australia, New Zealand, the US and Britain.

Adrian Harrington is head of funds management at Folkestone. This is an edited version of an article that first appeared in Cufflinks.

www.cufflinks.com.au

## When only an SMSF will do the business

TONY NEGLINE



The mis-selling of self-managed superannuation funds has been a problem for more than 10 years.

But strangely we hear much less about SMSFs when they produce a better outcome than other options — and a great argument would be needed not to use one.

This issue came to mind while I was reading a recent decision from the WA Supreme Court, *Cornell v Cornell*.

The background to the case is important — Phillip Cornell received damages of \$5.8 million after suffering major injuries in a workplace accident in 1999.

He contributed most of the proceeds to a large retail super fund and received a disability pension from that fund.

The pension wasn't reversionary — that is, in the event of his death, it wouldn't automatically be paid to one or more specified people.

In addition, when the pension started the fund didn't allow

binding death benefit nominations (BDBN) — that is, documents executed by fund members that ensure death benefit proceeds are paid to nominated beneficiaries or the deceased's estate.

In July 2010, Cornell died as a result of complications from his injuries. At the date of his death he had not completed a BDBN, although his super fund had permitted these nominations for a number of years. As a result, the large fund would automatically pay the money to his estate.

He had, however, completed a legal will in September 2004. This was structured to take into account the tax laws that applied to super before July 2007.

As a result, it contained many redundant clauses that ceased to have any relevance, which seems to have made the document unnecessarily long and complicated. Probate was granted on the estate three months after Cornell's death, with the primary beneficiary being his son Kieran Cornell, who was 15 when his father died.

Apart from the money in the super fund the estate had some real estate and other assets of modest value.

In 2013, Kieran and his mother, Julie Scott, asked that the super fund monies be paid as a pension to Kieran because it was

more tax effective than paying these proceeds to the estate. If the money had been paid to the deceased estate, then some super death benefit lump-sum tax would have been deducted before being distributed to the estate's beneficiaries, either directly or via a testamentary trust.

The executor was reluctant to

In addition, there is the attraction that the money is protected from creditors

act on this suggestion because one of the executor's primary jobs is to maximise the estate, as opposed to producing a better tax outcome for beneficiaries.

The executor solved this dilemma by asking the court for its thoughts on what was best.

It decided Kieran should receive the child pension from the large super fund.

As a so-called child death benefit pension, it will cease when Kieran turns 25 and any remaining account balance will be paid to him as a tax-free lump sum.

Any income from that non-super money will be taxed at normal marginal rates. Perhaps income splitting might be

available via a family trust, but if Kieran has children, minor children face high tax rates on any distributions.

A potentially better idea is for the child pension rules to say only modest income payments and no lump-sum withdrawals are permitted and the pension would automatically terminate before the child turns 25.

After termination the remaining account balance would then be paid from the super fund as a death benefit to the deceased's estate, and then either be gifted to a testamentary trust or super proceeds trust. The advantage here is income could be split between beneficiaries, and any income paid to minors would face normal adult tax rates. In addition, there is the attraction that the money is protected from creditors.

The strategy of paying minor children pensions is quite common. The problem is, large APRA-regulated super funds can't implement this more flexible solution, which means you would have to use a SMSF.

It would be foolish to ignore this aspect when assessing the merits or otherwise of using these types of funds.

Tony Negline is author of *The Essential SMSF Guide 2015-16* published by Thomson Reuters.

## A pathway to tax concessions

MONICA RULE



The idea that capital gains tax concessions even exist is enough to interest many investors — but it must be made clear they are only available in the context of self-managed superannuation funds where there is a small business involved.

Indeed, the great thing about being a small-business owner with a SMSF is you can transfer your business premises into it. In this situation you may also be eligible for generous CGT concessions, but you need to be careful.

First, to qualify as a small business, your turnover must be less than \$2 million, or the net asset value must not exceed \$6m.

Second, the business property must meet the active asset test.

To meet this test, the property must be owned for 15 years or less and active for a total of at least half the period from the acquisition date to the date of transfer, or the date the business ceased (if the transfer occurred within 12

months of the business ceasing). If the property is owned for more than 15 years, it needs to be active for a total of at least seven years from the acquisition date to the date of transfer, or the date the business ceased (if the transfer occurred within 12 months of the business ceasing).

If the transfer occurs more than 12 months after the business ceases, the active asset period ends when the transfer occurs, or when the business ceased if the commissioner of taxation grants an extension of time.

The business property does not need to be continuously active for the above periods as long as the active periods add up to the minimum periods. It also does not need to be active at the time of transfer as long as it is held ready for use in the business.

But it does need to be in a state of preparedness for use in the business and functionally operative. So if the property is still under construction, it is not held ready for use.

Active assets include real estate, equipment, machinery, goodwill, mining rights, intellectual property, or government licences.

Passive assets include shares, rent, loans, interests in trusts, annuities, royalties, and foreign exchange gains.

An issue that often arises with my clients is where their property has mixed uses — part of it is used in their business and part is leased to other businesses. If a property's main use is to derive rent, it can't be an active asset.

The tax office's publication TD 2006/78 provides guidance in determining whether the main use of a property is to derive rent.

The publication states that if a property is used partly for your business and partly to derive rent, it will be a question of fact dependent on all the circumstances as to whether the main use of the property at the time is to derive rent.

Things taken into consideration include the comparative areas of use of the premises (between deriving rent and other uses) and the comparative levels of income derived from the different uses of the property.

All uses are considered in determining what the main use of the property is and whether it is an active asset. But personal use by the property owner, or by an individual who is an affiliate, is not considered in determining the main use of the property.

Monica Rule is an SMSF specialist and author.

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