

Strategies available to cut capital gains tax

Moderate the amount payable on the sale of assets

SCOTT FRANCIS

Investors often seek to defer capital gains tax where possible ... because of capital gains tax. There are a number of strategies investors can examine.

The most obvious strategy, given the current tax rules, is to take advantage of the discount offered on capital gains where an asset is held for at least 12 months. In a superannuation fund, this means the tax rate will decrease from 15 per cent to 10 per cent on a realised (meaning the asset is sold) capital gain.

Outside superannuation a 50 per cent discount is applied to the capital gain once the asset is held for 12 months. These discounts significantly reduce the tax burden of a capital-gains tax event.

The capital gains tax arrangements have been in place for many

years though and it is worth noting that should an ALP government win power there is a plan to halve the current discount from 50 per cent to 25 per cent

In buying and selling assets such as shares, CGT is straightforward, but things can get a little more difficult with managed funds because very few publish after-tax returns. Any trading that goes on in a managed fund, for example if a large investor sells their units in the fund and shares have to be sold, potentially means capital gains passed on to unit holders as part of the fund distributions.

It takes some investigation by an investor to find out what different parts there are to the distribution they receive from their managed fund, potentially including interest income, fully franked income, unfranked income and capital gains.

In contrast, holding shares directly offer the investor greater control of capital gains tax events, even allowing them to make specific decisions related to their own circumstances (for example, delaying a sale in one financial year

because they know they will earn less income in the next year, and therefore face a lower tax rate).

Separately so-called managed accounts have grown in popularity, in part for their ability to offer investors control over capital gains — giving investors access to an investment management service, while owning the shares directly in their own name.

Super and CGT

Superannuation provides two key advantages for people looking to manage capital gains.

The first is that the lower tax regime of superannuation means any capital gains realised in superannuation “leaks” less tax compared to investments held in the name of someone on the average income tax rate or higher.

Keeping assets that have the expectation of capital gains in a superannuation fund makes sense — provided you can forgo access to these funds until you reach your preservation age. (The age at which you can access superannuation benefits.)

How the capital gains tax discount works

Purchase price of the shares	\$30,000
Sale price of the shares	\$50,000
Capital gain	\$20,000
Capital gain after 50% discount	\$10,000

Source: Eureka Report

Keeping assets that have the expectation of capital gains in a superannuation fund makes sense

This strategy makes even more sense for people with the ability to transfer assets from the “accumulation” phase of superannuation to the “pension” phase, where the tax rate for capital gains falls to 0 per cent.

Because of this, deferring capital gains tax sales until a superannuation fund is in pension mode is potentially a powerful strategy.

For those facing capital gains tax on assets outside of superannuation, the recent change to laws that allow people to claim a tax deduction for a personal contribution to superannuation provides a great way for people who face the 32.5 per cent income tax bracket or higher to more than halve their tax liability on the sale of an asset.

Consider the following scenario, based on the purchase and sale of shares that were held for a period of more than 12 months: the shares were purchased for \$30,000 and more than a year later sold for \$50,000; the capital gain was \$20,000 and the CGT after applying the discount was \$10,000.

Let’s assume that this person is paying income tax at the rate of 32.5 per cent. They face a tax liability of \$3250 based on the \$10,000 capital gains they have to add to their personal income from the sale of these shares (excluding Medicare).

However, if they make a tax-deductible contribution to superannuation of \$10,000, this effectively reduces their taxable income by the amount of the capital gain, so there is no tax payable outside of superannuation.

Instead, they would pay 15 per cent contributions tax, or \$1500, more than halving the tax payable. In thinking about this strategy, you do need to keep in mind the concessional superannuation contributions limits (now \$25,000 per annum).

An interesting element of capital gains tax for individuals is that the amount of the capital gain is added to their income — meaning that a person’s income tax bracket is a key element in the capital gains tax equation.

If there is an opportunity to realise a capital gain in a financial year where you have lower income tax, for example if you are having a career break or deferring the capital gain until after retirement, it may well be worth deferring a capital gain until then.

Similar to this, if you have a capital gain that increases your

taxable income into the next tax bracket in a financial year, it is worth considering whether deferring the asset sale into a year where you have less income, and therefore the gain will be taxed in a lower bracket, is a strategy worth thinking about.

In conclusion, the perfect scenario for investors is to own assets they don’t have to sell and that provide increasing income and value over time.

This, of course, is unrealistic and makes capital gains tax a reality for most investors. Thinking through the ownership of investments likely to provide capital gains, the timing of investment sales and looking to offset capital gains tax with tax-deductible superannuation contributions are all strategies that can be used to moderate the amount of tax payable on the sale of assets.

Scott Francis writes for Eureka Report, which is owned by financial services company InvestSMART.

www.investsmart.com.au

Amazon-resistant retail exposure

DIVIDEND DETECTIVE

Vicinity Centres

ASX CODE: VCX
SHARE PRICE: \$2.73
INDUSTRY: Real estate
FORECAST FY1
DISTRIBUTION: 16.3c

GARETH ABERNETHY

The Australian retail sector has been the focus of much heated debate in recent times. A combination of weaker than expected retail sales and the pending launch of Amazon Australia has investors running for the hills and “shorters” ramping up their bets that companies including JB Hi-Fi and Harvey Norman will disappoint the market. No doubt the likely outcome of Amazon’s arrival lies somewhere between the doomsayers and eternal optimists. It is likely the e-commerce giant will dampen industry margins, although for bigger-ticket items and the full retail experience, including food and entertainment, shopping centres should continue to play a pivotal part in the Australian retail market.

Vicinity Centres is one of the country’s largest owners and operators of shopping centres and retail assets. It owns and/or operates over 80 properties around the country valued at more than \$25 billion, with almost \$18bn in retail sales generated at its locations. Generally speaking, Vicinity’s assets are not considered tier-one — that is, centres located in prime locations and usually within capital city CBD locations. While not at the quality level of, say, Centrepunt Westfield, these assets are a long way from your country town malls, with locations such as the DFO outlets, Chatswood Chase and Chadstone. Vicinity has a geographically diverse range of assets, with Victoria its largest exposure, followed by NSW and Queensland.

Vicinity recently undertook an asset swap with GIC, trading the 49 per cent ownership of Chatswood Chase (while retaining management) for 50 per cent ownership of the Queen Victoria Building, Galleries and The Strand in the Sydney CBD — it also took over management of these assets. Given the lower aggregate quality of Vicinity’s portfolio when compared to some of its listed peers, this is a positive move that is both slightly accretive to earnings as well as highly productive with high sales per square metre.

Trading at a discount to its NTA of \$2.82 and undertaking a buyback, Vicinity (at about \$2.73) is an attractive addition to an income-oriented portfolio.

Gareth Abernethy is an analyst for the Clime Australian Income Fund.

www.clime.com.au

SMSF members can’t ignore dementia risk

MONICA RULE



What this means is the SMSF no longer meets the legal structure of an SMSF. Under the superannuation law, all members must be either an individual trustee or a director of the corporate trustee of an SMSF. A member with dementia has a legal disability so they are unable to perform these roles.

We read regularly the many variations on what a self-managed superannuation fund member should do to guard against the unfortunate things which could prevent them from managing their SMSF successfully. But today I want to look at one particularly difficult area: dementia.

Dementia is very prevalent among older Australians — the government’s own estimates suggest there are up to 400,000 people with dementia and about 1.2 million involved in the care of someone with dementia.

Most of the time advice on third-party management of your SMSF recommends putting in place an Enduring Power of Attorney so that the member can step down as an individual trustee (or a director of the corporate trustee) and the person with the EPA appointed to manage the SMSF.

An EPA is a legal agreement that enables a person to appoint a trusted person to make superannuation decisions on their behalf. It is made by choice and executed by anyone over the age of 18 who has full legal capacity.

However, if an SMSF member is already suffering from dementia, they do not have the full legal capacity to understand the implications of giving an EPA to another person.

Therefore, an EPA cannot be put in place. Family members may encounter situations where their loved ones suffering from dementia (normally an elderly mother or father) has an SMSF with quite a lot of assets but no one has an EPA to take over the management of the SMSF.

Monica Rule is an SMSF Specialist.
www.monicarule.com.au

Ramsay Health Care waiting in recovery

DAVID WALKER



A recent relief rally in Ramsay Health Care shares after the health services group AGM should reassure shareholders. Preceding days had seen a sell-off to as low as \$64.39 as the market priced in a downgrade to Ramsay’s 2018 earnings guidance.

The downgrade came after the insurance regulator APRA reported the number of people with private health insurance fell 17,000 in the September quarter following a decline of 10,000 in the June quarter. Ramsay was already out of favour after the guidance issued with the result fell short of the 11 per cent growth the market forecast for 2018. Short selling interest in the stock has risen. It is currently trading about \$67.00.

So what has been happening at one of the market’s best regarded stocks? Ramsay faces a “soft environment” for admissions, which is a product of minimal wages growth, household indebtedness, pressure on household disposable income — and our dysfunctional federation.

Where possible cash-strapped Australians are deferring elective surgery in private hospitals to avoid the expensive and sometimes unpredictable gap between the total cost and the health fund benefit, while public hospitals are competing for private patients to shift costs from state governments and their underfunded public health systems to private health funds and the commonwealth.

Of course Ramsay, a multinational company, is not restricted to Australia. However, the 2018 outlook is also difficult in Britain and France, which contributed around a third of 2017 earnings. The public health systems in these countries have progressively cut the “tariffs”, or rates paid



Ramsay Health Care is one of Australia’s largest healthcare businesses with a market capitalisation of about \$13.5 billion

to private hospitals for particular procedures, in return for greater volumes of outsourced work. An undersupply of nurses in Britain is inflating Ramsay’s costs there while uncertainty remains in France about the new policy towards public funding of private healthcare. Ramsay’s European earnings will be flat in 2017-18 before resuming incremental growth in 2018-19 after Britain’s National Health Service increases tariffs in April 2018.

It seems the market is once again focusing on short-term problems at the expense of longer-term accelerating growth. A wave of greater demand for hospital care from the ageing baby boomer cohort is expected from 2020, and forecasts for the increase in demand continue to be upgraded.

In expecting a guidance downgrade the market also possibly missed the significance of the pro-

urement cost savings Ramsay is extracting from suppliers. The group is already one of the world’s five largest operators of private hospitals. These savings, operating leverage and new revenue from brownfields expansion (capacity additions to existing hospitals) are why Ramsay is able to grow at high single digit in 2018 when industry volume growth in Australia is low single digit and European earnings are flat.

There is another reason to like Ramsay: a sad one but one the market possibly does not yet appreciate. Ramsay is Australia’s largest private provider of mental health services, with 25 facilities and 900 beds.

Every Australian family would know someone who has suffered mental illness. The need for more mental health services is further underlined by a disturbing statistic we heard last week: among Australian women under 30 ac-

cessing private healthcare, there are now more annual admissions to mental hospitals than to wards for pregnancy and childbirth. This partly reflects the increasing average age at which women give birth but is mainly due to the incidence of mental illness in young people and better diagnosis and referrals.

Ramsay is engaged in the mental health sector and wants to do more. This year it opened a new facility on the Gold Coast to address the shortfall of services there. Under the government’s reforms to private health insurance last month, patients with limited mental health cover will be able to upgrade their cover to access in-hospital mental health services without serving a waiting period. All the trends point to increasing demand for mental health services — where Ramsay is positioning itself.

The simplification of private

health policies under the reforms, and the discounts for insureds under the age of 30, should restore some coverage. The surge in private patients in public hospitals is unsustainable because it inflates public waiting lists and private premiums. It will be addressed in the next National Health Agreement.

I believe the disappointments and share price volatility of recent months will turn out to be a long-term buying opportunity. Our model portfolio trimmed its position in Ramsay in June after the stock ran up to \$75, above our estimate of value around \$72. In September, after the result and guidance disappointment, we rebuilt the position as low as \$61.20. We still think the stock is worth \$72 in 2018 rising to \$82 in 2019.

David Walker is ASX Large-Caps Portfolio Manager at Clime Asset Management.

THE AUSTRALIAN

LIMITED TIME SUBSCRIPTION OFFER

12-month subscription at \$10 per week.
Min cost of \$520 for over \$615 worth of value*

Subscribe now 1300 135 514
 theaustralian.com.au/google

Get every story plus a Google Home. Just \$10 a week.



RRP \$199

Get news from *The Australian* read to you with a voice-activated personal assistant

- Ask Google for weather forecasts and traffic updates
- Control and enjoy your music with voice commands^
- Manage your day and set reminders

*12 month plan subscription offers to be billed as follows – The Australian Digital Subscription \$40 billed every 4 weeks for the first 12 months, total minimum cost of \$520; The Australian Digital Subscription + The Weekend Australian (delivered Saturday) \$40 billed every 4 weeks, total minimum cost of \$520. No cancellations during the first 12 months. At the end of the 12 month plan period, subscriptions will automatically renew to recurring 4 week periods at \$40, unless cancelled. Customers can cancel after the initial 12 month contract subject to full terms and conditions. Offer includes a Google Home device (requires Wi-Fi, a Google account and a compatible device). Controlling certain devices and features in your home requires a compatible smart device. Supported Operating System is Android 4.1 and higher, iOS 8.0 and higher. Google Home cannot be exchanged (unless faulty), nor redeemed for cash. Only one Google Home per email address and per person. We will supply your contact details to Harvey Norman Business & Education, who will deliver the Google Home device only to your Australian registered subscription address and will email you with dispatch details. Google Home only available for delivery to Australian address captured and will require a signature. Available only for a limited time or until stock lasts. Not in conjunction with any other offer. New customers only. Offers are not available to any person who has previously breached any of our subscription terms and conditions. Home Delivery offers are only available where normal home delivery exists and not where additional freight is ordinarily charged. Full offer terms and conditions apply - see www.theaustralian.com.au/subscription terms for full details. ^To access music on Google Home you will require either a Spotify or Google Play account.