

## You can claim your share trading as a deduction

TONY NEGLINE



Our tax laws typically allow a deduction for business expenses. Of course, the deductions must relate to what in the eyes of the tax office is a business, as opposed to some form of financial activity.

Occasionally, people try to argue that their past-times and hobbies are businesses, so that their costs become business expenses.

It is possible to run a share-trading business?

The short answer is yes, unless we're talking about a super fund formed after June 2011. From that date, super funds were banned from declaring for tax purposes that they were operating a share-trading business.

For many individual taxpayers, the situation can be tricky, as demonstrated by a recent Administrative Appeals Tribunal case.

Neelam Devi has been in Australia for almost 10 years and always worked in the childcare sector, in which she holds various qualifications from Indian universities and Australian institutions.

She started trading shares in 2010 using family savings of \$60,000 and a \$40,000 CBA margin loan. In 2011, she earned about \$40,000 from her work and in her spare time traded shares. During the 2010-11 financial year, she had made 71 share-purchase transactions with a value of just under \$380,000 and 37 sales with a value of \$215,000.

Most of these transactions occurred before December 2010, with only 10 taking place during 2011. During that year, she received only \$4400 in dividends before taking into account franking credits and other tax impacts. By the end of the year, she owned seven stocks with a then market value of just under \$45,000.

The key issue here is that during the 2011 financial year she made a \$20,000 trading loss, which she wanted to claim as a tax deduction because she believed she was running a share-trading business.

She claimed to be involved in share trading during 2011 and wanted to gradually increase her profits from this so that it became her full-time occupation.

She initially explained that she spent between five and 10 hours a week on this activity, but then subsequently increased this to between 15 hours and 25 hours. The AAT found this sudden increase in time difficult to accept.

Initially, Devi had told the ATO she didn't have a business plan, but then sometime later produced a single-page document about trading strategies and disaster plans and so on. The AAT decided that this document was produced after the end of the 2011 financial year.

Based on her oral evidence, the AAT decided that Devi knew "very little about the share transactions that she claimed to have personally extensively researched and undertaken ... she was unable to provide any

### For many individual taxpayers, the situation can be tricky

details ... even in the broadest terms". In addition, she couldn't identify any of the companies she had invested in or the industries in which they operated.

The AAT found her excuses inadequate and concluded that it was probably her husband who had performed the research and, most likely, the transactions themselves.

Typically, the AAT looks at a number of factors, including the following, to determine if a taxpayer is conducting a share-trading business: repetition and regularity in buying and selling shares; turnover; whether the taxpayer is operating to a plan such as setting budgets and keeping records; maintaining an office; shares are accounted for on a gross receipts (that is, before any taxes or expenses); and whether the taxpayer was engaged in a full-time profession.

In her favour, the AAT found that Devi invested a large sum and ran her own office at home. On all the other factors, it said, she failed. Consequently, Devi lost her case — and the ability to claim the trading loss of \$20,000.

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

## Bouyant Buffett's three top tips

The legend's latest letter lists insights for the private investor

ELIZABETH REDMAN



If Warren Buffett is worried about global markets' choppy start to 2016, he isn't showing it.

It's more likely the Berkshire Hathaway chairman — who sent out his legendary letter to shareholders this week — isn't worried at all.

He's famous for encouraging investors to be fearful when others are greedy — when markets are rising strongly — and greedy when others are fearful, snapping up bargains as prices plunge.

With the US benchmark Dow Jones Industrial Average off 4.5 per cent so far this year, Buffett's latest letter stops short of encouraging a buying spree.

But he does offer a number of insights for the private investor worth keeping in mind whether markets are falling or rising.

**You will make mistakes.** Buffett is ready to admit his own errors, even though he is widely considered the most successful living investor.

Berkshire Hathaway's share price has compounded at a rate of 20.8 per cent annually over the period from 1965 to 2015. This is a return many fund managers could only dream of, and more than double the average annual return of the S&P 500 (including dividends) of 9.7 per cent over the same period.

"I've made some dumb purchases," he writes to shareholders. "We've also had some winners — a few of them very big."

Among the Buffett conglomerate's retail and manufacturing operations, he points out that some businesses report returns above 100 per cent, others return about 12 per cent to 20 per cent. A few have "very poor" returns.

"We are now paying the price for my misjudgements," he writes. "I will commit more errors; you can count on that."

But the division as a whole returned 18.4 per cent, a very respectable result indeed.

Private investors can take



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'I've made some dumb purchases. We've also had some winners — a few of them very big,' writes Warren Buffett

comfort in the knowledge that even Buffett makes mistakes, and the total return of a well-diversified portfolio is more important than the embarrassment of an occasional bad pick.

**Look beyond dividends.** Of course, self-directed Australian investors, particularly those in retirement, are right to consider the yield that different investments offer.

Yet yield isn't the only factor to consider, as many resources investors recently showed when they accepted BHP Billiton's decision to cut its dividend to avoid a situation where it would have to take on more debt to meet payout obligations.

Even though payout ratios in the US are usually lower due to differences in the tax system, Berkshire Hathaway reported a total of about \$US1.8 billion of dividends from its investments in American Express, Coca-Cola, IBM and Wells Fargo.

But these companies also retain a proportion of earnings, which "fund business opportunities that usually turn out to be

### Ten year performance of Warren Buffett's Berkshire Hathaway group



advantageous", Buffett writes. "If gains do indeed materialise, dividends to Berkshire will increase."

For private investors, it's worth examining current and prospective investments to see which companies are paying out such a high proportion of their earnings that they will struggle to reinvest for growth. The companies that pay a more modest dividend now and keep some capital to plough into worthwhile projects could see returns increase over time.

**Stay focused on the long term.** Buffett is well known as an opti-

mist on the long-term health of the US economy. "For 240 years it's been a terrible mistake to bet against America, and now is no time to start," he writes.

"The babies being born in America today are the luckiest crop in history."

As Buffett suggests, children in his upper-middle-class neighbourhood now have a better standard of living than oil tycoon John D Rockefeller Sr did at the time Buffett was born.

Workers are now able to produce more by working more

efficiently, leading to "staggering" growth in GDP per capita.

Berkshire's businesses are focused on long-term trends, too. For instance, Berkshire Hathaway Energy has invested \$US16bn in renewable energy and committed to more as the world moves towards cleaner sources of energy.

The BNSF railway uses almost four litres of diesel to move a tonne of freight about 800km, which Buffett says makes it four times as fuel-efficient as trucks.

On the question of climate change's possible effects on the insurance businesses, Buffett writes that policies can be re-priced annually to reflect changing risks.

Much ink has been spilt during the past two months over the sharp falls in sharemarkets around the world.

Buffett offers a refreshing reminder to private investors of the importance of remembering how investments have already performed over a long period, and then looking ahead to the likely key trends over the decades to come.

## Would you know what to do if you lost the ability to manage your super fund?

MONICA RULE



One thing self-managed super fund investors might not consider is what to do when they lose the capacity to take care of their affairs.

There are more than 350,000 Australians living with dementia. With about 42 per cent of SMSF members aged 55 and over, it is a looming issue for many ageing SMSF trustees. Would you know what to do should you lose the ability to run your SMSF?

One option, which my surprise you, is to retain the SMSF. While the loss of mental capacity means an SMSF member can no longer make decisions for their SMSF, they can appoint someone to take on their trustee responsibilities.

The law allows a legal personal representative (LPR) who holds an enduring power of attorney (EPOA) to be appointed as a trustee or a director of the corporate trustee in place of the member.

An EPOA is a document that allows one person to give another authority to make decisions on their behalf. Be aware that an EPOA does not simply allow someone to act on behalf of the member; the member must resign as trustee or director of the corporate trustee and the LPR be appointed.

The LPR must consent in

writing to the appointment. The person appointed cannot be a disqualified person and must sign within 21 days of the appointment a declaration stating they understand their duties as trustee. It should be someone who is trustworthy, over 18 and with the mental capacity to make decisions.

A person who accepts the EPOA must understand the legal position they are putting themselves in and the member must understand the EPOA gives the LPR power to make decisions for the SMSF. The power of attorney can come into effect immediately or when (or if) the SMSF member becomes incapable of making decisions.

The SMSF's trust deed must allow for the appointment of the person, holding the EPOA, as a trustee. The resignation of the

member as a trustee or director of the corporate trustee must be in accordance with the trust deed, the superannuation law and other relevant laws. If the trustee is a company, the SMSF needs to comply with the company's constitution and the Corporations Act with respect to replacing directors.

Each state and territory has different laws for powers of attorney, so regard must be given to specific provisions to ensure the EPOA is valid. The SMSF must also lodge a change-of-details document with the ATO and ASIC.

All documents must be sighted by the SMSF's auditor at the annual audit of the SMSF. If the SMSF has individual trustees, there may be additional costs involved in changing the legal ownership of the SMSF's assets

because of the new trustee. Changes to the legal ownership of assets are not necessary if the SMSF has a corporate trustee.

The next option, and probably the most obvious choice, is to wind up the SMSF by rolling money into a retail super fund.

Most retail super funds have a range of investment options. Some allow assets such as listed shares to be transferred to them. Others will allow only cash — which means assets would need to be sold.

If the SMSF is in accumulation phase, the sale of assets will trigger capital gains tax. If the SMSF is in pension phase, no CGT is payable on the sale of assets supporting the pension.

The last option is not something of which many SMSF inves-

tors are aware. You could convert the SMSF into a Small APRA Fund (SAF). An SAF is similar to an SMSF, but instead of the member being the trustee a licensed trustee is responsible for running the superannuation fund. If an SAF contravenes the superannuation law, the member is not liable.

Like SMSFs, SAFs can acquire a broad range of assets and use similar investment strategies. SAFs offer the flexibility of an SMSF, but without the trustee responsibilities.

CGT is avoided when switching to an SAF. This is because only the trustee changes. The superannuation fund continues uninterrupted and does not dispose of any assets. Moving to an SAF might help retain investments such as shareholdings, investment

properties or business real property, so this is a good option for SMSF investors who want to keep existing investments.

I would encourage SMSF members, of all ages, to consider carefully what you will do if you can no longer run your SMSF.

Should the worst happen and you no longer have the mental capacity to manage your affairs, understanding the options available will give you the peace of mind that your retirement savings are protected and you will have some security in your twilight years.

*Monica Rule is the author of The Self Managed Super Handbook — Superannuation Law for Self Managed Superannuation Funds in plain English. www.monicarule.com.au*

### FLOAT WATCH

## Cash in on Candy Crush mania

### Sugar Dragon Limited

ASX code: SDC  
Shares on offer: 16 million  
Listing price: 20c  
Market capitalisation: \$5.7 million  
Listing date: March 21

SIMON HERMANN

One of the best known and most addictive games on Facebook is King.com's Candy Crush Saga, which is estimated to make more than \$US600,000 per day. While the game is played around the world, it is particularly popular in Asian countries: a recent survey found that every seventh person in Hong Kong regularly plays the smartphone game.

The Candy Crush Saga was released on Facebook in April 2012 and as a mobile application for smartphones in November 2012 by King Digital Entertainment. King Digital went public in 2014 to list on the NYSE in a \$US7 billion initial public offering, only to be recently acquired by Activision Blizzard for \$US5.9bn.

As with every successful franchise, the sale of the primary product is usually accompanied by complementary merchandising. Hong Kong-based Okmno Asia Limited has a licensing agreement with King.com to manufacture and distribute Candy Crush-branded confectionary in Asia. Okmno is a confectionary wholesaling business with manufacturers in China and Germany and Okmno has sold over 26 tonnes of Candy Crush-branded confectionary products in South Korea and Taiwan to date. The licence also covers Hong Kong, Macau and mainland China.

The coming listing of Sugar Dragon Limited provides investors with speculative exposure to demand for the Candy Crush-branded confectionary products in Asia as the company holds a 72.5 per cent interest in Okmno. Sugar Dragon seeks to raise \$3.2m to fast-track production and marketing of its confectionary products. The funds will be used to undertake further product designs, increase production, develop marketing channel partnerships but also to explore new opportunities.

Even though the licensing agreement is non-exclusive, Okmno is currently the only licensee in the region, resulting in a competitive advantage for being the "first mover".

However, IPO investors need to be aware that the listing is speculative in nature as Sugar Dragon has a limited operating history. The company is expected to remain reliant on external capital to fund its daily operations.

The company is highly dependent on its licence agreement with needs to be renewed by the end of 2017.

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