Your

Knowledge

August 2021

Selby Watson & Co. CHARTERED ACCOUNTANTS

We are here to help, contact us today:

Selby Watson & Co
Phone 02 6921 4219
Web www.selbywatson.com.au
Email admin@selbyco.com.au

KNOWLEDGE SHOP

Afterpay's $39bn pay day

Business advisers will tell you that you need to begin a business with the end in mind; a phrase popularised by Michael Gerber in *E-Myth*.

The announcement of the intended sale of Australian born fintech company Afterpay, pioneer of the 'buy now, pay later' platform, is a case in point.

The company was founded in 2015 by Nick Molnar and Anthony Eisen, listing on the ASX for $1 per share in May 2016. In 2017, they hit 1 million customers and 7,200 merchants, launched into New Zealand, and merged with Touchcorp Limited. A year later in 2018, they entered the US market. In 2019, it was the UK under the brand name Clearpay. In 2020, Hong Kong listed Chinese tech giant Tecent paid $300m for a 5% equity stake. By then, Afterpay boasted 5 million active US customers, 1 million in the UK. In this same year they took the opportunity to launch into Canada. In 2021, Afterpay announced the purchase of tech group Pagantis by their UK subsidiary in preparation for their launch into Europe.

Afterpay was also exceptionally well placed for the dramatic COVID-19 shift in consumer behaviour that supercharged online retail. As at 30 June 2021, the company had 16.2 million active customers (63% growth on 2020) and over 98,000 merchants (77% growth on 2020). When COVID-19 struck, Afterpay's share price dipped to a low of $12.44 on 20 March 202 but by 19 February 2021, hit a high of $151.92 ($96.99 at 30 June 2021). At 30 June, (unaudited) group revenue was $925m, growing 78% on the previous period (of which merchant revenue was $822m). However, growth comes at a cost with the 31 December 2020 half year results showing an after-tax loss of over $79m

Continued over…

(joining a long list of unprofitable tech companies such as AirBnb, Pinterest, DropBox, Slack and Uber).

The rise of Afterpay has been extraordinary; a combination of a game changing concept delivering consumer flexibility and the ability for merchants to grow their customer base with the potential of increasing per transaction values, all backed by an aggressive expansion plan. They are a brand that became a verb.

On 2 August, the announcement was made that US financial services and digital payments giant Square, had agreed to acquire all of the issued shares in Afterpay for approximately US$29 billion (A$39 billion). The sale is expected to be all in stock and Nick Molnar and Anthony Eisen will join Afterpay as employees in first quarter of 2022.

For many innovative and fast growth companies, sale is the end game - generally to another company in the same or similar market with strong synergies that is willing to pay a premium for the opportunity. Afterpay has achieved that in spectacular style. And, you can see the appeal of a business model that is replicable, utilises unique systems and technology, is adaptable, and has proven its ability to grow and expand globally.

The model

For consumers, Afterpay offers a way of spreading the cost of purchases over four payments across six weeks. No fees are charged unless the payment is late. If a payment is late, an initial $10 late fee is charged, and a further $7 if the payment remains unpaid 7 days after the due date. For each order below $40, a maximum of one $10 late fee may apply per order. For each order of $40 or above, the total of the late fees that may be applied are capped at 25% of the original order value or $68, whichever is less.

While free to consumers (unless they pay late), Afterpay charges merchants a 30 cent fee, plus a commission ranging from 4% to 6% to the merchant. Payments transacted through Afterpay take 48 hours to be delivered in full to the merchant.

The fee structure, and the fact that Afterpay makes spending easier for consumers to rationalise, has not been without controversy. A Senate committee and the Payments System Review explored whether more consumer protections, such as customer credit checks, were needed. However, neither review wanted to stifle the growth of financial competition or innovative fintechs, leaving regulation to market forces. At present, late fees represent less than 10% of the company's revenue.

Afterpay store cards are available in the US and other markets. And, in July this year, Money by Afterpay launched in Australia and New Zealand with Afterpay staff trialling the product ahead of a full-scale launch anticipated in October 2021.

What if you have Afterpay shares?

The sale of Afterpay has a number of hurdle points including regulatory approval from the Foreign Investment Review Board and approval of the shareholders of both Afterpay and Square.

If the transaction proceeds then Afterpay shareholders will have two main options. They can either receive NYSE-listed Square shares or they could receive shares in Square that are listed on the ASX. This is because Square will establish a secondary listing on the ASX allowing Afterpay shareholders to trade Square shares via CHESS Depositary Interests (CDIs) on the ASX.

Afterpay state that the transaction is intended to be tax-free for Australian shareholders electing to receive NYSE-listed Square shares or CDIs. Among the conditions precedent is a ruling from the Australian Taxation Office (ATO) for Australian shareholders to apply scrip-for-scrip capital gains tax (CGT) rollover relief. If the rollover applies, then the cost base and acquisition date of the Square shares will basically remain the same as your Afterpay shares. **- End -**

Lockdown Support Update

The support available to individuals and business has been constantly evolving and changing. Here's a summary of where support stands around the country.

For individuals

From 2 August 2021, the COVID-19 Disaster Payment has increased to a maximum of $750 per week for those who have lost 20 hours of work or more, and $450 for those who have lost between 8 and 20 hours of work. In most cases, the payment now applies from day 1 of a lockdown. In general, you need to be living in, or impacted by Commonwealth declared lockdown to receive the payment although some States have funded an extension of the payment beyond hotspot areas.

A special separate $200 a week 'top-up' payment has been added for those currently receiving an income support payment through social security, ABSTUDY Living Allowance, Dad and Partner Pay or Parental Leave Pay in addition to their existing payment, if they can demonstrate they have lost more than 8 hours of work and meet the other eligibility requirements for the COVID-19 Disaster Payment. The payment was put in place because people receiving income support payments are not eligible for the COVID-19 Disaster payment.

New South Wales business

In New South Wales, the following grants and payments are accessible:

- Up to $100,000 in weekly JobSaver cashflow support payments. Payments are based on 40% of your NSW payroll payments. Eligible businesses without employees that meet the eligibility criteria (such as sole traders with no employees), can access a payment of $1,000 per week.
- Up to $15,000 through the expanded NSW 2021 COVID-19 business grants program
- NSW micro-business grants

The decline in turnover test required for the JobSaver, COVID-19 business and micro-business grants has been causing a lot of angst but some additional flexibility has been provided. Businesses and non-profit entities can now pass this test if they can show a decline in turnover of at least 30% due to the Public Health Order over a minimum 2-week period within the relevant test period compared to:

- The same period in 2019;
- The same period in 2020; or
- The 2-week period immediately before the start of the relevant test period.

The test period depends on which payment you are looking at:

- COVID-19 business grant: 26 June 2021 to 17 July 2021 (this is changed to 27 May 2021 to 17 July 2021 for entities on the NSW border with Victoria);
- JobSaver and the micro-business grant: 26 June 2021 until the Greater Sydney lockdown ends.

This additional flexibility is helpful for businesses that started after the comparison period in 2019 and for those that have undertaken an acquisition, disposal or restructure.

Queensland business

$5,000 Business Support Grants are available for those impacted by the lockdown from Saturday, 31 July 2021. Your business does not have to be in the local government areas locked down but needs to be impacted by it. To access the grant, you will need to show a decline in turnover of at least 30%. The grants are available to businesses with a turnover of $75,000 or more and annual Queensland payroll of less than $10 million. Applications open mid-August. See Business Queensland for details.

South Australia

Grants of $3,000 for employing businesses and $1,000 for non-employing businesses are available to businesses that experienced a decline in turnover of at least 30% as a result of the health restrictions from 20 July 2021. The grants are available to those with a turnover of $75,000 or more and Australia wide payroll of less than $10 million. See COVID-19 Business Support Grant – July 2021 for details.

More funding for Victorian SMEs

There are two main streams for grants in Victoria:

- Those who qualified for the Business Costs Assistance Program Round Two or the Licensed Hospitality Venue Fund 2021; and
- Businesses that previously did not access grants

Existing grant beneficiaries

If your business previously received the Business Costs Assistance Program Round Two or the Licensed Hospitality Venue Fund 2021, additional grants of $2,800 for the Business Costs Assistance Program Round Two and up to $20,000 for the Licensed Hospitality Venue Fund 2021 have been announced. Your business cannot retrospectively apply for these grants. See Helping Victorian Businesses Who Need It Most.

New grants

For businesses that did not access previous grants, the Business Costs Assistance Program Round Two July Extension offers grants of $4,800 for employing and non-employing business depending on your sector. For those in the hospitality sector, a new Licensed Hospitality Venue Fund 2021 July Extension is available offering grants of up to $7,200 for each eligible premises. Applications for both grants close 13 August 2021.

A new Small Business COVID Hardship Fund grant of up to $8,000 has been announced for businesses that are not eligible for existing support funding. To access the grant, your business must be severely impacted by the COVID-19 lockdowns with a decline in turnover of 70% or more. No further details are available at present.

Other support

For Alpine businesses, additional grants between $5,000 and $20,000 will be available to 430 Alpine based businesses. See the Alpine Resorts Winter Support Program (closes 20 August 2021).

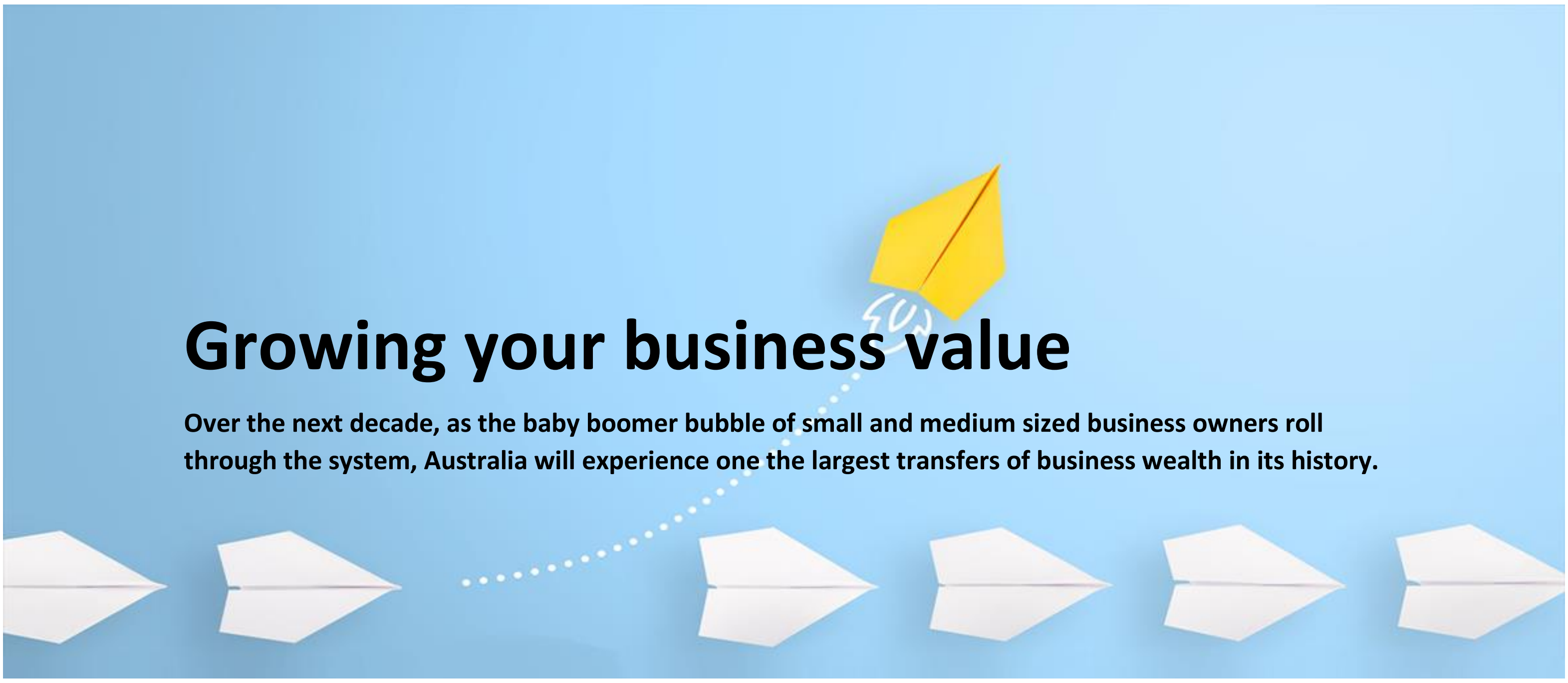
Rent relief for commercial tenants is also now in place for businesses that have suffered a decline in turnover of at least 30% as a result of COVID-19. Landlords will be required to provide proportional rent relief in line with a business's reduction in turnover and mediation is available through the Victorian Small Business Commission. A hardship fund will be established for landlords providing rent relief although no details are available as yet.

Please contact us if you would like support to prepare for, or to access, the support you need.

Quote of the month

"You may have to fight a battle more than once to win it."

Margaret Thatcher, former British Prime Minister



Growing your business value

Over the next decade, as the baby boomer bubble of small and medium sized business owners roll through the system, Australia will experience one the largest transfers of business wealth in its history.

Succession planning is more important than ever. Not just because of the transfer of wealth, but because of the polarising impact of high supply and low demand on the saleable value of a business.

Australia is expected to see the retirement age of baby boomers peak over the coming decade. The basics of the law of supply and demand suggest that as supply increases, prices will be driven downwards. For SMEs however, there is a much greater probability we will see a dramatic polarisation in the price of SMEs for sale. High quality businesses command premium prices while low quality businesses will be highly price sensitive and, in some cases, unsaleable.

If your children are not offering you a retirement strategy, selling your business can be difficult if there are not obvious competitors or complimentary businesses knocking on your door for your market share or unique offering.

Forward planning for succession is a critical issue for SME owners who want to exit their business over the coming decade. This planning, with an adequate timeframe, allows you to actively enhance the value of your business.

Most business owners have a view on what their business might be worth and the factors that influence business value. The key question then is, what do you need to focus on to enhance business value for a potential buyer? There are four key areas: growth, capacity, profitability and risk.

Growth

Buyers will generally pay a premium for a built-in level of growth. Growth, if well managed, will produce increased profits. So, a potential buyer knows that the revenue stream they are purchasing with the business, comes with a growth increment. Not only does this growth factor offer future profit increments it also insulates the business against the ‘what if’ factor. Any major change in a business causes a disconnect and these disconnect events can impact revenues and profits. Built in growth offers some protection against this.

Capacity

Provides for both the present and capability to facilitate growth in the future. Areas where capacity needs to exist includes infrastructure, systems capability, and management capability. Systems and management are often the areas given the least amount of focus, yet they are the very areas where value can be leveraged and enhanced the most. One of the reasons why franchises command price premiums is because they offer a level of systems and management. These same factors can be built into any business.

Profitability

A history of profits and strong cashflows are normally the two greatest influences on SME business value. When assessing your profitability, you need to compare yourself at two levels. First compare your performance against the top quartile of your industry sector. Top quartile businesses always attract higher valuations. Then, look outside your own business sector. Measure your Return on Investment (ROI). Buyers of your business will not only be comparing you with your industry. They may be looking for investment return more than they are looking for a specific business. So, in a potential sale you may be competing with a business from another industry to secure your buyer. You should be looking for a ROI in excess of 25%.

Risk Management
Business owners are becoming more sensitive to risk. Strong corporate governance and risk management policies will enhance business value. Buyers will be looking for a history of compliance and a risk management culture. Risk management can include the existence of current employment contracts, operating licences, customer and supplier agreements and OH&S procedures.

These four areas will normally be high on the business value hierarchy and the areas where change can most significantly impact on business value.

If business succession is on your agenda, you need to assess your business under these criteria. Where your performance or position is below what it needs to be, you can identify the issues that you need to focus on to change your business value.

This process may not simply mean the difference between an ordinary sale price and a good price. It may be the difference between a sale that releases your business capital or no sale at all.

Talk to us about succession planning for your business that makes a difference.

Are COVID-19 grants and funding tax free?

Most people would think that money provided by the Government to support people and business during a crisis would be tax free? Otherwise, it's like giving money with one hand and then taking it away with the other, isn't it?

But, the tax laws don't work like that. To make a payment tax-free, legislation is required to enable it to be classified as exempt income or non-assessable non-exempt income. In general, any income received will be assessable unless the Government has legislated for it to be tax-free. JobKeeper for example was not tax free and anyone who received it in 2020-21 will need to declare it in their income tax return.

At the Federal Government level, the Prime Minister recently announced that the COVID-19 Disaster Payment will be tax free and legislation enabling this change is before Parliament. Other payments however, such as Pandemic Leave Disaster Payment, remain taxable.

The Treasurer has also been granted the power to make State and Territory grants tax-free but only from 13 September 2020, and only if they request the Commonwealth Government to make it tax free. If you're confused, it's not surprising. The result is a mix of tax treatments depending on what support you received and from whom. To date, only a series of Victorian business grants are tax-free (but we expect more will be made tax free).

The general rule is that grants are likely to be taxable unless they are specifically excluded from tax. If the grant relates to your continuing business activities, then it is likely to be included in assessable income for income tax purposes. The position can be different in cases where the payment is made so that the entity can commence a new business or cease carrying on a business but there will still often be some tax implications.

-End-