McMillanShakespeareGroup

ASX ANNOUNCEMENT

FY13 RESULTS GUIDANCE AND THE PROPOSED FBT CHANGES

MMS expects to deliver a FY13 net profit after tax in the range of $61m to $63m. The midpoint of the preliminary indicative result represents an increase on FY12 of 15%. This guidance is subject to finalisation and audit by the Company's external auditors.

As previously announced by MMS, on 16 July 2013 the Federal Government proposed legislative changes to the treatment of fringe benefits tax (FBT) on motor vehicles. As the industries' stakeholders were not consulted on the proposed FBT changes they have taken MMS by surprise and as a result MMS, its employees, its shareholders and its customer base of not for profit institutions, charities and public and private sectors find themselves in an uncertain business, investment and service environment which MMS considers is not likely to be resolved with sufficient certainty or clarity until after the outcome of the Federal election. For various reasons, including the significant industry disruption and uncertainty, the Company requested of ASX an extension of the voluntary suspension from trading of the Company's securities but this request was rejected.

The proposed changes, which abolish the twenty eight year old practice of being able to rely on the statutory formula method to quantify the amount of FBT payable on employer provided motor vehicles (as introduced in 1986 by the then Federal Labor Government), is creating disruption within the industry and is expected to lead to an unknown and unquantifiable decrease in demand for novated leases and an adverse impact to the business overall. The statutory formula method was the subject of a detailed review and recommendation in the Henry Tax review which commented that:

> "*While the operating cost method provides a more accurate valuation than the statutory formula, it imposes a high compliance burden for users with low levels of business use.*"
>
> *"While market valuation would be appropriate for most fringe benefits, a statutory formula for car fringe benefits should be retained to reduce compliance costs in the medium-term. The Review has carefully considered a range of options to enhance the operation of the statutory formula, from increasing the number of gradations in the formula to basing the taxable value of a vehicle on its emissions rating. It favours replacing the statutory formula with a single statutory rate that would apply to the original cost of the car regardless of the distance travelled. This approach would provide a more neutral taxation treatment for employee remuneration by reducing the concessions available to those who can take their income as a private car benefit."*

The Henry Tax review went on to make the following recommendation:

> *"The current formula for valuing car fringe benefits should be replaced with a single statutory rate of 20 per cent, regardless of the kilometres travelled."*

This recommendation was subsequently adopted by the Federal Labor Government and passed into law with a commencement date of 10 May 2011.

As the proposed legislative changes apply to novated leases entered into after 16 July 2013 the Company believes (and the early evidence is) that its ability to originate novated leases may be significantly impacted from this date. The proposed changes require the passing of legislation to become effective and if enacted will have a material adverse impact on the future earnings of MMS.

The amount of this impact will be dependent on the outcome of the pending Federal election and whether the proposed legislative changes will be passed as law following the election. The Government appears determined to pass the amendments if it is elected but may not have a majority in the Senate. The Opposition has publicly stated it is opposed to the measure and will not pursue it if elected. The resulting uncertainty is such that the Company is not currently in a position to provide any earnings guidance. The Company is working through various scenarios, including the potential structural changes to internal departments should the proposed legislative changes be enacted as law. Any changes required and the resultant influence on margins will also be affected by the relationship between the run off of annuity income and the revenue streams not directly impacted by the proposed changes.

In addition, given the uncertainty caused by the proposed legislative changes and their impact on MMS, the Company is not currently in a position to provide any guidance on any final dividend payment for the year ended 30 June 2013.

MMS expects to release its full year results for FY13 on 27 August 2013.

The preliminary indicative results are summarised as follows by segment:

	GRS	AM	Unallocated	Total
	$m	$m	$m	$m
Revenue	156	173	2	331
Pre tax profit pre-UK	67	22	1.2	89
Segment net profit after tax pre-UK	47	15	0.9	63
UK share of JV and acqusition costs	0	-0.5	0	-0.5
Net profit after tax	47	14.5	0.9	62
(GRS - Group Renumeration Services, AM - Asset Management)				

Proposed legislative changes

The proposed legislative changes are expected to materially and adversely impact the Group Remuneration Services (GRS) segment which provides salary packaging and novated leasing products to the Not for Profit (NFP), charity, state and federal government and private sectors.

The revenue streams potentially adversely directly impacted are:

- revenue derived upfront (GRS Upfront Revenue) at the time a novated lease is settled including finance, insurance and ancillary commission revenue. The GRS Upfront Revenue from these sources included in the FY13 preliminary results is $81m. The proposed legislative changes impacting this revenue stream would apply to novated leases written after 16 July 2013; and

- revenue derived over the term of a salary packaged novated lease (GRS Annuity Motor Vehicle Revenue) including:
  - salary packaging fees relating to the packaging of the motor vehicle;
  - fleet management fees for managing the novated lease;
  - interest earned on funds related to salary packaged motor vehicles;
  - finance trail commission received from third party financiers from novated leases originated; and
  - commissions on motor products supplied to customers during the term of the salary packaged novated lease.

The amount of revenue from GRS Annuity Motor Vehicle Revenue included in the preliminary results is $23m which under the proposed legislative changes would be, if enacted, likely to decrease each year over the contract duration.

The proposed legislative changes do not apply to existing novated leases and committed orders on and prior to 16 July 2013 provided the existing individual lease arrangements do not materially change after 16 July 2013. Subject to MMS retaining the employer salary packaging contract, the revenue from this source will continue to be earned until such time as the lease ceases, either by early termination of the novated lease, the end of the leasing term or termination of the employees' service with the employer. The existing portfolio of novated leases will run down in line with occurrence of the events described above. The profile of this run off will be dependent on the contracts retained by MMS, the term of the lease and the employee continuing employment with the employer.

The GRS revenue streams not directly impacted by the proposed regulatory changes described above is revenue derived from salary packaging non motor vehicle items (GRS Non Motor Vehicle Revenue). Revenue from this includes those derived from the NFP and charity sector. The amount of revenue from GRS Non Motor Vehicle Revenue included in the preliminary indicative results is $52m.

The NPAT margin in respect of the FY13 preliminary results for the GRS segment is approximately 30%. The majority of the GRS costs to drive the three GRS sources of revenue described above are not solely attributable to one of these three sources but are shared across the three revenue streams. The Company is therefore not currently in a position to provide any guidance on its novated lease income stream. However, the Company expects the incremental contribution to NPAT margin from novated leases is higher than the GRS 30% NPAT margin and therefore any decline in novated lease revenue will, in isolation, be likely to decrease the GRS NPAT margin below the FY13 level.

The Company is currently undertaking work to further understand the GRS margin impact from the proposed legislative change as well as any potential impacts the proposed legislation may have on the carrying value of the Company's assets.

In respect of the Asset Management (AM) segment the proposed legislative changes require those customers who provide motor vehicles to staff and use the statutory fraction to migrate to use the log book for orders entered after 16 July 2013, other than for exempt vehicles including certain vans and utilities that have incidental private use. A number of existing AM customers are using the operating costs method (log books). The proposed FBT changes do not directly impact the overall AM segment business plan and strategies that the Group had in place before the changes were announced.

MMS is the largest salary packaging company in the Australian market and through this market position has been able to generate significant cash reserves. At 30 June 2013 MMS had cash of $57m and had significant headroom over its banking covenants, including a Company interest cover ratio of c.9.2:1 at 30 June 2013 vs a 3:1 banking covenant. All drawdowns under our banking facilities have been utilised to fund assets in the AM segment with a gearing ratio of c.60% of the asset book at 30 June 2013 vs an 80% banking limit. The cash generation of the Company is likely to be impacted adversely by a significant decrease in novated lease settlements that have occurred and is likely to continue to occur since the Federal Government's announcement of the proposed legislative changes on 16 July 2013.

Given the significant change in the value proposition of a novated lease for an employee MMS is not in a position to forecast potential future demand.

The Company is fortunate to have a dedicated and talented team of staff. Based on current cash headroom and until there is more clarity in regard to the legislative outcomes the Company intends to retain all permanent staff including those who are directly engaged in originating novated leases. The Company is actively managing paid and unpaid leave to minimise the financial impact on the Company during this time. Should the proposed legislative changes not proceed, MMS will have a team with the requisite skills to maintain a strong competitive position.

Current political position

The Federal Opposition leader, Tony Abbott, announced on Friday, 19 July 2013 that if the Liberal National Party Coalition win the upcoming Federal election there will be no alterations to the current FBT scheme and it will not support the proposed legislative changes in Opposition. As it appears unlikely that the Government will enact legislation to give effect to its proposed legislative changes before the election, their implementation will be contingent on whether or not the current Federal Government wins the upcoming election and has sufficient majority in Parliament after the election to pass its proposed legislative changes. Accordingly, there is considerable uncertainty as to whether the proposed legislative changes to the current FBT scheme will eventuate.

Next steps

In the meantime, the Company continues to work assiduously with all relevant stakeholders to ensure those proposed legislative changes do not proceed in their current form.

The Company will provide further updates and guidance as it becomes aware of material changes and developments in relation to its operations and financial circumstances and the proposed legislative changes. In the meantime, given the present uncertainty MMS will suspend all communications with investment analysts, shareholders, the press etc until after the election unless the position becomes clearer prior to then.

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About McMillan Shakespeare

McMillan Shakespeare is considered a market leader in the provision of remuneration programs. Its services include remuneration policy design, salary packaging benefit administration and motor vehicle lease management backed by expertise in FBT management, tax and compliance. McMillan Shakespeare also provides a complementary fleet management service, including the procurement of motor vehicles and finance and the management of fuel card and service maintenance programs.