Smartgroup Corporation Ltd
Half-year report

30 June 2017

ABN 48 126 266 831

Contents

Market release

22 August 2017
ASX Market Announcements Office
ASX Limited
20 Bridge Street
Sydney, NSW, Australia, 2000

Smartgroup Corporation Ltd - Results for announcement to the market

In accordance with the Listing Rules, Smartgroup Corporation Ltd encloses for immediate release the following information:

1. Appendix 4D,
2. Review of operations, and
3. Smartgroup Corporation Ltd half-year report 2017.

Smartgroup Corporation Ltd will conduct a briefing on the results at 8:30 am (Sydney time) on 23 August 2017.

Amanda Morgan
General Counsel and joint Company Secretary

Appendix 4D

Statutory results for announcement to the market

	$000's
Revenue from ordinary activities	up $34,529 (57%) to $95,182
Profit from ordinary activities after tax attributable to the owners of Smartgroup Corporation Ltd	up $3,348 (25%) to $16,784
Net profit for the period attributable to the owners of Smartgroup Corporation Ltd	up $3,348 (25%) to $16,784

Dividend information	Amount per share (cents)	Franked amount per share (cents)	Tax rate for franking credit
Final 2016 dividend per share (paid 31 March 2017)	15.0	15.0	30%
Interim 2017 dividend per share (to be paid 29 September 2017)	16.5	16.5	30%

The record date for determining entitlement to the interim dividend is 15 September 2017.
There is no dividend reinvestment plan in place.

Net tangible assets	30 June 2017	31 December 2016
Net tangible assets per ordinary security, cents per share*	(80.91)	(76.90)

The net tangible assets per ordinary share is calculated based on 119,611,272 ordinary shares on issue as at 30 June 2017 (31 December 2016: 118,446,559 ordinary shares), which excludes the 3,469,133 shares outstanding and unvested issued under the 2015, 2016 and 2017 long-term incentive plans (31 December 2016: 3,040,492).

Control Gained Over Entities

On 2 May 2017, a wholly owned group entity, Advantage AccessPay Pty Ltd, acquired 100% of the ordinary shares of AccessPay Pty Ltd, Fleet Solutions Pty Ltd and 50% of the ordinary shares of AccessPay Payroll Solutions Pty Ltd. Refer to note 5a for details on the acquisition.

	Reporting entity's percentage holding		Contribution to profit	
Details of Associates and Joint Venture Entities	**30 June 2017 %**	**30 June 2016 %**	**30 June 2017 $000**	**30 June 2016 $000**
Health - e Workforce Solutions Pty Ltd	50%	50%	89	229

Independent auditor's review

The financial report for the half-year ended 30 June 2017 has been reviewed by PricewaterhouseCoopers and there is no review dispute or qualification.

** Net tangible assets are calculated based on net assets excluding goodwill at 30 June 2017 of $231,976,000 (31 December 2016: 217,453,000) and intangible assets at 30 June 2017 of $60,132,000 (31 December 2016: $68,070,000).*

Review of operations

	Consolidated		
	30 June 2017 $'000	Restated 30 June 2016 $'000	Movement %
Revenue	**95,182**	**60,653**	**57%**
Share of after tax profits of joint ventures accounted for using the equity method	89	229	-61%
Fair value loss on revaluation of financial liabilities	(6,271)	-	n/a
Expenses			
Employee benefits expense	(35,638)	(24,564)	45%
Administration and corporate costs	(11,278)	(7,849)	44%
Advertising and marketing expenses	(1,705)	(1,165)	46%
Occupancy expenses	(1,901)	(1,320)	44%
Other expenses	(366)	(685)	-47%
Earnings before interest, tax, depreciation and amortisation (EBITDA)	**38,112**	**25,299**	**51%**
Depreciation expense	(716)	(579)	24%
Amortisation expense^	(8,224)	(4,772)	72%
Net finance costs	(2,345)	(753)	211%
Profit before income tax for the half-year	**26,827**	**19,195**	**40%**
Income tax expense^	(10,043)	(5,759)	74%
Net profit after income tax for the half-year	**16,784**	**13,436**	**25%**
Add: Amortisation, tax effected	5,857	3,441	70%
Add: Cash tax benefit on deductible amortisation^	1,381	1,289	7%
Add: M&A costs	52	410	-87%
Add: Fair value loss on revaluation of financial liabilities	6,271	-	n/a
Net profit after tax and amortisation (NPATA) *^	**30,345**	**18,576**	**63%**
EBITDA margin	40%	42%	-2 pts
NPATA margin	32%	31%	1 pt
Net cash inflow from operating activities***	**26,056**	**15,950**	**63%**
Net cash inflow as a percentage of NPATA***	86%	86%	n/a
	Cents	**Cents**	
NPATA per share **	24.6	15.5	58%
Dividends declared per share **	16.5	9.8	68%

^ 2016 amortisation expense, income tax expense, cash tax benefit on deductible amortisation and NPATA have been restated following final acquisition accounting for Advantage.

** NPATA reflects the net profit after tax, adjusted to exclude the non-cash tax-effected amortisation of intangibles and significant non-operating items.*

*** NPATA per share and Dividends declared per share are based on the number of shares estimated to be 123,526,516 shares (30 June 2016: 119,533,800 shares), which includes the 3,469,133 shares held by the Company under the Loan Funded Share Plan (LFSP) (30 June 2016: 3,040,492 shares) and 446,111 shares to be issued to Selectus vendors by September 2017 as deferred consideration (30 June 2016: nil).*

**** Net cash inflow from operating activities excludes receipts and payments related to customer salary packaging bank accounts.*

Financial performance

The half-year 2017 financial results for Smartgroup Corporation Ltd and its controlled entities ('the Group') show continued growth in revenue and earnings. Revenues of $95.2m represent growth of 57% over half-year 2016, while Earnings Before Interest, Tax, Depreciation and Amortisation (EBITDA) grew 51% to $38.1m.

The half-year 2017 Net Profit After Tax and Amortisation ('NPATA') of $30.3m (excluding after-tax merger and acquisition costs and fair value adjustments of $6.3m) represents growth of 63% over half-year 2016.

Revenues have increased primarily due to higher novated leasing settlements and revenues and the inclusion of Autopia (acquired in July 2016), Selectus (acquired in August 2016) and AccessPay (acquired in May 2017).

Review of operations (cont'd)

Operations

The acquisitions of Advantage, Autopia and Selectus have extended the Group's reach into the charity and aged care, corporate and rebatable (predominately private schools) sectors. The Group has successfully transitioned multiple supply agreements from the acquired businesses, including for novated lease financing, insurance and vehicle consumables, to Group supply arrangements.

The Group continued its focus on operational excellence to retain and grow its client base. Of note, all major client contracts across the group up for renewal in 2017 have been renewed. We continue to engage with our clients at multiple levels to ensure strong ongoing relationships. In addition, with our recent acquisitions, we have instituted a cross-sell program to ensure that we bring our full range of relevant services to each client to further deepen and broaden these relationships.

Following these acquisitions, the Group is working to harmonise all People and Safety frameworks, to ensure that it continues to retain and attract high quality employees with a commitment to customer service excellence.

Acquisitions

AccessPay Group (AccessPay)

On 2 May 2017, the Group completed the acquisition of AccessPay Group for $14.7m in cash, funded from existing cash reserves, and $0.3m in shares. AccessPay, based in Adelaide, provides salary packaging services principally to clients in the Public Benevolent Institutions sector across Australia. It manages approximately 40,000 salary packages for approximately 500 employer clients.

Post balance date events

Selectus Pty Ltd (Selectus) deferred consideration

In July 2017, the Group entered into agreements with two of the previous shareholders of Selectus whereby deferred share consideration, payable under the terms of the sale agreement, would be settled by the Group in cash in lieu of shares, at the equivalent of $6.56 per share. The relevant shareholders held 79.07% of the shares in Selectus at the time of the sale.

Based on the Selectus performance for the twelve months to 30 June 2017, the total deferred share entitlement of the Selectus vendors is 2,131,442 shares. Of this, 79.07% (1,685,331 shares) will be settled in cash at $6.56 ($11.1m) and the remaining 20.93% (446,111 shares) will be issued by September 2017. In addition, cash in lieu of dividends foregone of $0.8m will be paid to vendors by September 2017.

Equity issuance

The total shares on issue at the date of this report is reconciled by:

Balance as at 30 June 2017 (including LFSP) – Note 7	123,080,405
Plus: share issue for Selectus deferred consideration	446,111
	123,526,516

Directors' report

The directors present their report, together with the financial statements, on the consolidated entity (referred to hereafter as the 'Group') consisting of Smartgroup Corporation Ltd (referred to hereafter as the 'Company' or 'parent entity') and the entities it controlled at the end of, or during the half-year ended 30 June 2017.

Directors
The following persons were directors of the Company for the half-year ended 30 June 2017 and up to the date of this report, unless otherwise stated.

Michael Carapiet (Chairman)
Deven Billimoria
John Prendiville
Gavin Bell
Andrew Bolam
Ian Watt
Deborah Homewood

Principal activities
During the half-year the principal activities of the Group consisted of outsourced administration, being primarily salary packaging, novated leasing, software, distribution and Group services and fleet management services.

Review of operations
The profit after tax for the Group is $16,784,000 (30 June 2016: $13,436,000). Refer to the Review of operations for further commentary on the results.

Dividends
On 22 August 2017, the directors declared a fully-franked dividend of 16.5 cents per ordinary share. The record date is 15 September 2017 and the dividend will be paid on 29 September 2017.

Auditor's independence declaration
The auditor's independence declaration is included on page 7 of the half year report.

Rounding of amounts
The Company is of a kind referred to in ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191, issued by the Australian Securities and Investments Commission, relating to 'rounding off'. Amounts in this report have been rounded off in accordance with that instrument to the nearest thousand dollars, or in certain cases, the nearest dollar.

This report is made in accordance with a resolution of directors.

On behalf of the directors,

Michael Carapiet
Chairman
22 August 2017
Sydney

Auditor's Independence Declaration

As lead auditor for the review of Smartgroup Corporation Ltd for the half-year ended 30 June 2017, I declare that to the best of my knowledge and belief, there have been:

(a) no contraventions of the auditor independence requirements of the *Corporations Act 2001* in relation to the review; and

(b) no contraventions of any applicable code of professional conduct in relation to the review.

This declaration is in respect of Smartgroup Corporation Ltd and the entities it controlled during the period.

Sam Hinchliffe	Sydney
Partner	22 August 2017

PricewaterhouseCoopers, ABN 52 780 433 757
One International Towers Sydney, Watermans Quay, Barangaroo NSW 2000,
GPO BOX 2650 Sydney NSW 2001
T: +61 2 8266 0000, F: +61 2 8266 9999, www.pwc.com.au

Consolidated statement of profit or loss and other comprehensive income

For the half-year ended 30 June 2017

	Notes	Consolidated 30 June 2017 $'000	Restated * 30 June 2016 $'000
Revenue		95,182	60,653
Share of after tax profits of joint ventures accounted for using the equity method		89	229
Fair value loss on revaluation of financial liabilities	5c	(6,271)	-
Expenses			
Employee benefits expense		(35,638)	(24,564)
Administration and corporate costs		(11,278)	(7,849)
Depreciation expense		(716)	(579)
Amortisation expense		(8,224)	(4,772)
Advertising and marketing expenses		(1,705)	(1,165)
Occupancy expenses		(1,901)	(1,320)
Other expenses		(366)	(685)
Net finance costs		(2,345)	(753)
Profit before income tax		26,827	19,195
Income tax expense		(10,043)	(5,759)
Net profit for the half-year attributable to the owners of Smartgroup Corporation Ltd		16,784	13,436
Other comprehensive loss for the half-year, net of tax			
Items that may be reclassified subsequently to profit or loss			
Net change in fair value of cash flow hedges taken to equity, net of tax		(363)	(200)
Other comprehensive loss for the half-year, net of tax		**(363)**	**(200)**
Total comprehensive income for the half-year attributable to the owners of Smartgroup Corporation Ltd		16,421	13,236
Profit attributable to:			
Owners of the parent		16,784	13,436
Non-controlling interests		-	-
		16,784	13,436
Total comprehensive income attributable to:			
Owners of the parent		16,421	13,236
Non-controlling interests		-	-
		16,421	13,236

Earnings Per Share		**Cents**	**Cents**
Basic earnings per share	9	14.03	12.89
Diluted earnings per share	9	13.95	12.71

** Refer to note 1 for finalisation of comparative period acquisition accounting which has resulted in comparatives being restated.*
The above consolidated statement of profit or loss and other comprehensive income should be read in conjunction with the accompanying notes.

Consolidated statement of financial position

As at 30 June 2017

	Notes	Consolidated 30 June 2017 $'000	Consolidated 31 December 2016 $'000
Assets			
Current assets			
Cash and cash equivalents		50,653	79,990
Restricted cash and cash equivalents	11	39,853	39,493
Trade and other receivables		15,745	15,885
Other current assets		6,314	7,025
Total current assets		112,565	142,393
Non-current assets			
Property and equipment		3,588	3,150
Investments accounted for using equity method		6,088	6,751
Goodwill	4	231,976	217,453
Intangible assets		60,132	68,070
Other non-current assets		512	508
Derivative financial instruments		-	307
Deferred tax asset		1,117	-
Total non-current assets		303,413	296,239
Total assets		415,978	438,632
Liabilities			
Current liabilities			
Trade and other payables		24,220	26,427
Customer salary packaging liability	11	39,853	39,493
Income tax payable		4,355	8,848
Provisions		6,733	5,550
Deferred consideration	5c	15,811	9,541
Other current liabilities		3,122	1,336
Total current liabilities		94,094	91,195
Non-current liabilities			
Deferred tax liability		-	175
Derivative financial instruments		142	-
Provisions		1,687	1,636
Borrowings		123,486	150,118
Contingent consideration	5c	1,244	1,244
Total non-current liabilities		126,559	153,173
Total liabilities		220,653	244,368
Net assets		195,325	194,264
Equity			
Issued capital	7	173,055	170,940
Reserves	8	3,018	2,631
Retained profits		19,252	20,693
Total equity		195,325	194,264
Equity attributable to owners of the parent		195,283	194,264
Non-controlling interests		42	-
Total equity		195,325	194,264

The above consolidated statement of financial position should be read in conjunction with the accompanying notes.

Consolidated statement of changes in equity

For the half-year ended 30 June 2017

Consolidated	Issued capital $'000	Reserves $'000	Retained profits $'000	Total equity $'000	Non controlling interest $'000	Attributable to owners of the parent $'000
Balance at 31 December 2015	62,013	11,664	8,828	82,505	-	82,505
Restated profit after income tax for the half-year *	-	-	13,436	13,436	-	13,436
Other comprehensive income for the half year, net of tax	-	(200)	-	(200)	-	(200)
Total comprehensive income for the half-year	-	(200)	13,436	13,236	-	13,236
Transactions with owners in their capacity as owners:						
Shares issued on business combination	10,360	(10,360)	-	-	-	-
Share-based payments	-	477	-	477	-	477
Dividends paid	-	-	(9,022)	(9,022)	-	(9,022)
Restated balance at 30 June 2016	72,373	1,581	13,242	87,196	-	87,196
Balance at 31 December 2016	170,940	2,631	20,693	194,264	-	194,264
Profit after income tax for the half-year	-	-	16,784	16,784	-	16,784
Other comprehensive income for the half year, net of tax	-	(363)	-	(363)	-	(363)
Total comprehensive income for the half-year	-	(363)	16,784	16,421	-	16,421
Transactions with owners in their capacity as owners:						
Shares issued on business combination	300	-	-	300	-	300
Share-based payments	1,815	750	-	2,565	-	2,565
Dividends paid	-	-	(18,225)	(18,225)	-	(18,225)
Non-controlling interests arising on acquisition	-	-	-	-	42	-
Balance at 30 June 2017	173,055	3,018	19,252	195,325	42	195,283

** Refer to note 1 for finalisation of comparative period acquisition accounting which has resulted in comparatives being restated.*
The above consolidated statement of changes in equity should be read in conjunction with the accompanying notes.

Consolidated statement of cash flows

For the half-year ended 30 June 2017

		Consolidated	
			Restated *
	Notes	**30 June 2017**	**30 June 2016**
		$'000	**$'000**
Cash flows from operating activities			
Receipts from customers		103,608	65,576
Payments to suppliers and employees		(60,479)	(41,564)
Interest received from operations		1,388	590
Interest paid		(2,701)	(1,002)
Income taxes paid		(15,760)	(7,650)
		26,056	15,950
Receipts of restricted cash		578,388	395,315
Payments of customer salary packaging liability		(576,626)	(394,669)
Net cash inflow from operating activities		27,818	16,595
Cash flows from investing activities			
Net proceeds received from investments		332	75
Proceeds from joint venture		750	-
Payments for purchase of property and equipment		(163)	(184)
Payments for business combination (net of cash acquired)	5a	(14,509)	(1,708)
Net cash used in investing activities		(13,590)	(1,817)
Cash flows from financing activities			
Proceeds from long term incentive plan		2,020	195
Repayment of borrowings		(27,000)	(5,920)
Dividends paid		(18,225)	(9,022)
Net cash used in financing activities		(43,205)	(14,747)
Net (decrease)/increase in cash and cash equivalents		(28,977)	31
Restricted cash and cash equivalents at the beginning of the year		39,493	749
Cash and cash equivalents at beginning of the year		79,990	19,546
Cash and cash equivalents at end of the half-year		50,653	18,932
Restricted cash and cash equivalents at the end of the half-year	11	39,853	1,395
Total		**90,506**	**20,327**

** Comparatives restated for presentation of receipts and payments related to customer salary packaging bank accounts.*

The above consolidated statement of cash flows should be read in conjunction with the accompanying notes.

Notes to the financial statements

Note 1. Basis of preparation

Smartgroup Corporation Ltd ('the Company') is a company limited by shares, incorporated and domiciled in Australia. The financial report covers the consolidated entity (referred to hereafter as the 'Group') consisting of the Company and the entities it controlled for the half-year ended 30 June 2017.

The consolidated half-year financial report is a general purpose financial report prepared in accordance with Australian Accounting Standard Board ('AASB') 134 'Interim Financial Reporting' and the Corporations Act 2001.

This half-year financial report does not include all the notes of the type normally included in an annual financial report. Accordingly, this report is to be read in conjunction with the annual report for the year ended 31 December 2016 and any public announcements made by the Company during the interim reporting period in accordance with the continuous disclosure requirements of the Corporations Act 2001.

The financial statements have been prepared on the basis of historical cost, except for the revaluation of certain non-current assets and financial instruments. Cost is based on the fair values of the consideration given in exchange for assets. All amounts are presented in Australian dollars, unless otherwise noted.

The Company is of a kind referred to in ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191, issued by the Australian Securities and Investments Commission, relating to 'rounding off'. Amounts in this report have been rounded off in accordance with that instrument to the nearest thousand dollars, or in certain cases, the nearest dollar.

The principal accounting policies adopted are consistent with those of the previous financial year and corresponding interim reporting period.

Comparative period restatement

On 11 December 2015, the Group acquired 100% interest in Salary Packaging Solutions Pty Ltd and National Tax Manager Pty Ltd, which together operate as Advantage Salary Packaging ('Advantage'), for a total consideration of $58,543,000. On 29 January 2016, the Group completed an agreement with Trinity Management Group Pty Ltd ('TMG') to acquire selected assets of TMG.

At 30 June 2016, the acquisition accounting of Advantage and TMG was provisionally determined. At 31 December 2016, the provisional accounting for Advantage was finalised and valuation of customer contracts for TMG was completed, resulting in reclassification from goodwill to intangible assets of $16,000,000, relating to Advantage customer contracts and $1,500,000 for TMG customer contracts. As a result, the comparative profit and loss has been restated to recognise amortisation on customer contracts of $1,733,333 and $178,242 for Advantage and TMG respectively, for the interim period to 30 June 2016. Details of all adjustments on finalisation of Advantage acquisition accounting are disclosed in the annual report for the year ended 31 December 2016.

New, revised or amending Accounting Standards and Interpretations adopted

The Group has adopted all of the new or amended Accounting Standards and Interpretations issued by the Australian Accounting Standards Board ('AASB') that are mandatory for the current reporting period. The adoption of these Accounting Standards and Interpretations did not have any significant impact on the financial performance of the Group for the half year ended 30 June 2017 (and 30 June 2016) or financial position of the Group as at 30 June 2017 (and 31 December 2016).

Impact of standards issued but not yet adopted

(a) AASB 15 Revenue from contracts with customers

The AASB has issued a new standard for the recognition of revenue. This will replace AASB 118 which covers revenue arising from the sale of goods and the rendering of services. The Group will adopt the new standard from 1 January 2018. Had the Group adopted the new standard from 1 January 2017, the Group estimates that it would not have a significant impact to the amounts recognised in the financial statements as the Group is considered to be an agent in most service arrangements.

(b) AASB 16 Leases

AASB 16 was issued in February 2016. It will result in almost all leases being recognised on the balance sheet, as the distinction between operating and finance leases is removed. The standard will primarily affect the accounting for the Group's operating leases. The group has not yet determined to what extent non-cancellable operating lease commitments, as at the reporting date, will result in the recognition of an asset and a liability for future payments and how this will affect the Group's profit and classification of cash flows. Some of the commitments may be covered by the exception for short-term and low-value leases and some commitments may relate to arrangements that will not qualify as leases under AASB 16. The standard is mandatory for first interim periods within annual reporting periods beginning on or after 1 January 2019. At this stage, the group does not intend to adopt the standard before its effective date.

(c) AASB 9 Financial instruments

AASB 9 addresses the classification, measurement and derecognition of financial assets and financial liabilities, introduces new rules for hedge accounting and a new impairment model for financial assets. The group has decided not to adopt AASB 9 until it becomes mandatory on 1 January 2018. The group does not expect the new guidance to have a significant impact on the classification and measurement of its financial assets and financial liabilities. The derecognition rules have been transferred from AASB 139 and have not been changed. The new hedge accounting rules will align the accounting for hedging instruments more closely with the Group's risk management practices. The Group is currently assessing the potential impact of the new impairment model.

Notes to the financial statements (cont'd)

Note 2. Dividends

On 22 August 2017, the directors declared a fully-franked dividend of 16.5 cents per ordinary share. The record date is 15 September 2017 and the dividend will be paid on 29 September 2017. This dividend has not been included as a liability in these financial statements. The total estimated dividend to be paid is $20,379,000.

Note 3. Operating segments

Identification of reportable operating segments

The Group has identified its segments based on the internal reports that are reviewed and used by the Chief Executive Officer and Chief Financial Officer (who are identified as the Chief Operating Decision Makers ('CODM')) in assessing performance and in determining the allocation of resources. There is no aggregation of operating segments.

The CODM reviews EBITDA (Earnings Before Interest, Tax, Depreciation and Amortisation). The accounting policies adopted for internal reporting to the CODM are consistent with those adopted in the financial statements.

Types of products and services

The principal products and services of each of these operating segments are as follows:

Outsourced administration ('OA')	This part of the business provides outsourced salary packaging services, which includes novated leasing, the marketing of salary packaging debit cards, share plan administration and outsourced payroll services.
Vehicle services ('VS')	This part of the business provides end-to-end fleet management services.
Software, distribution and group services ('SDGS')	This part of the business provides salary packaging software solutions, distribution of vehicle insurances and workforce management software to the healthcare industry.

Intersegment transactions

Intersegment transactions were made at market rates. Intersegment transactions are eliminated on consolidation.

Intersegment receivables, payables and loans

Intersegment loans are initially recognised at the consideration received. Intersegment loans receivable and loans payable that earn or incur non-market interest are not adjusted to fair value based on market interest rates. Intersegment loans are eliminated on consolidation.

	OA $'000	VS $'000	SDGS $'000	Intersegment eliminations / Corporate $'000	Total $'000
Half-year ended 30 June 2017					
Revenue					
Sales to external customers	82,907	2,245	9,622	-	94,774
Intersegment sales	-	1,202	7,648	(8,850)	-
Total sales revenue	82,907	3,447	17,270	(8,850)	94,774
Finance revenue	408	-	-	-	408
Total Revenue	83,315	3,447	17,270	(8,850)	95,182
Segment results (EBITDA)	34,937	1,809	11,443	(10,077)	38,112
Depreciation					(716)
Amortisation					(8,224)
Finance costs (net)					(2,345)
Consolidated profit before income tax					26,827
Income tax					(10,043)
Consolidated profit after income tax					16,784
30 June 2017					
Assets					
Segment assets	147,896	10,695	12,159	245,228	415,978
Consolidated total assets					415,978
Liabilities					
Segment liabilities	62,201	4,685	3,859	149,908	220,653
Consolidated total liabilities					220,653

Notes to the financial statements (cont'd)

Note 3. Operating segments (cont'd)

	OA $'000	VS $'000	SDGS $'000	Intersegment eliminations / Corporate $'000	Total $'000
Half-year ended 30 June 2016 (restated)					
Revenue					
Sales to external customers	51,325	1,978	7,332	-	60,635
Intersegment sales	-	1,128	5,910	(7,038)	-
Total sales revenue	51,325	3,106	13,242	(7,038)	60,635
Finance revenue	18	-	-	-	18
Total Revenue	51,343	3,106	13,242	(7,038)	60,653
Segment results (EBITDA)	18,619	1,285	9,088	(3,693)	25,299
Depreciation					(579)
Amortisation					(4,772)
Finance costs (net)					(753)
Consolidated profit before income tax					19,195
Income tax					(5,759)
Consolidated profit after income tax					13,436
31 December 2016					
Assets					
Segment assets	145,492	10,245	15,711	267,184	438,632
Consolidated total assets					438,632
Liabilities					
Segment liabilities	70,609	7,140	6,317	160,302	244,368
Consolidated total liabilities					244,368

Note 4. Goodwill

	30 June 2017 $'000	31 December 2016 $'000
Gross carrying amount		
Balance at beginning of the period	217,453	90,867
Adjustments resulting from business combinations occurring during the period (note 5a)	14,523	126,586
Balance at end of the period	231,976	217,453
Net book value		
At the beginning of the period	217,453	90,867
At the end of the period	231,976	217,453

Notes to the financial statements (cont'd)

Note 5. Business combinations

5a. Current period acquisitions

AccessPay Group ('AccessPay')
On 2 May 2017, the Group acquired 100% of the ordinary shares of AccessPay Pty Ltd, Fleet Solutions Pty Ltd and 50% of the ordinary shares of AccessPay Payroll Solutions Pty Ltd ('AccessPay') for total consideration of $15,000,000. AccessPay, based in Adelaide, provides salary packaging services principally to public benevolent institutions across Australia and manages approximately 500 employer clients. The goodwill of $14,523,000 represents the synergies expected to be obtained by the Group from this acquisition. The acquired business contributed revenues of $1,584,000 and net loss after tax of $76,000 to the Group for the period from 2 May 2017 to 30 June 2017. If the acquisition occurred on 1 January 2017, the full half year contributions would have been revenues of $4,473,000 and loss after tax of $262,000 subject to adjustments arising as a result of purchase price allocation.

The acquisition was settled in cash of $14,700,000 and an issue of 46,225 ordinary shares for $300,000 to one of the vendors. These shares are escrowed and will be released in two tranches in 2018.

The values identified for the acquisition are provisional as at 30 June 2017.

Details of the acquisition are as follows:

	Fair value $'000
Cash and cash equivalents	191
Trade receivables	125
Other current assets	91
Plant and equipment	991
Other intangibles	276
Deferred tax asset	324
Trade and other payables	(706)
Employee provisions	(609)
Other provisions	(15)
Provision for income tax	(191)
Net assets acquired	**477**
Goodwill	14,523
Acquisition date fair value of consideration transferred	
Representing:	
Cash	14,700
Shares issued at $6.49 per share	300
	15,000
Acquisition costs	74
Cash used to acquire business, net of cash acquired:	
Cash paid to vendor	14,700
Less: cash and cash equivalents	(191)
Net cash used	14,509

Notes to the financial statements (cont'd)

Note 5. Business combinations (cont'd)

5b. Comparative period acquisitions

Trinity Management Group
On 29 January 2016, the Group acquired selected assets of TMG for total consideration of $2,952,000. At 31 December 2016, the valuation of customer contracts was completed, resulting in a reclassification from goodwill to intangible assets of $1,500,000. The business combination was finalised in the current financial period and did not result in adjustments to provisional acquisition accounting at 31 December 2016.

Autopia Group Pty Ltd ('Autopia')
On 4 July 2016, the Group acquired 100% of the ordinary shares of Autopia for the total consideration of $40,430,000. The business combination was finalised in the current financial period and did not impact the comparative period statement of profit or loss and other comprehensive income and statement of financial position.

Selectus Pty Ltd ('Selectus')
On 2 August 2016, the Group acquired 100% of the ordinary shares of Selectus for the total consideration of $132,800,000. The business combination was finalised in the current financial period and did not impact the comparative period statement of profit or loss and other comprehensive income and statement of financial position.

Details of the comparative period acquisitions are summarised as follows:

	31 December 2016			
	Autopia Fair Value $'000	**Selectus Fair Value $'000**	**TMG Fair Value $'000**	**Total Fair Value $'000**
Cash and cash equivalents	6,923	74	-	6,997
Restricted cash and cash equivalents	7,921	28,605	-	36,526
Trade receivables	668	2,699	270	3,637
Other current assets	-	1,757	-	1,757
Plant and equipment	139	445	-	584
Intangible assets	13,897	32,651	1,500	48,048
Deferred tax asset	-	-	-	-
Trade and other payables	(1,124)	(3,304)	-	(4,428)
Customer salary packaging liability	(7,921)	(28,605)	-	(36,526)
Provision for income tax	(875)	(539)	-	(1,414)
Deferred tax liability	(903)	(2,100)	(523)	(3,526)
Employee benefits	(818)	-	(25)	(843)
Other provisions	-	(1,216)	-	(1,216)
Net assets acquired	**17,907**	**30,467**	**1,222**	**49,596**
Goodwill	22,523	102,333	1,730	126,586
Acquisition date fair value of consideration transferred	40,430	132,800	2,952	176,182
Representing:				
Cash	40,180	89,266	1,708	131,154
Shares	250	32,424	-	32,674
Contingent consideration	-	11,110	1,244	12,354
	40,430	132,800	2,952	176,182
Acquisition costs	572	2,293	31	2,896
Cash used to acquire business, net of cash acquired:				
Cash paid to vendor	40,180	89,266	1,708	131,154
Less: cash and cash equivalents	(6,923)	(74)	-	(6,997)
Less: restricted cash and cash equivalents	(7,921)	(28,605)	-	(36,526)
Net cash used	25,336	60,587	1,708	87,631

Notes to the financial statements (cont'd)

Note 5. Business combinations (cont'd)

5c. Deferred and Contingent Consideration

Deferred consideration – Selectus

For the 12 month period to 30 June 2017, Selectus achieved an Adjusted EBITDA of $14,737,000 and satisfied other operational performance metrics which, together with the increase in the Company share price from $6.28 at 31 December 2016 to $7.17 at 30 June 2017, has increased the final consideration payable at 30 June 2017 to $15,811,000. As a result, a fair value loss of $6,271,000 is recognised in the profit and loss for the period ended 30 June 2017 and because of its non deductibility for tax purposes, the fair value loss has resulted in a increase in the effective tax rate of the Group at 30 June 2017.

Contingent consideration – TMG

In the event profit before tax (PBT) exceeds $864,000 for the year ended 31 December 2018 additional consideration may be payable. The fair value of contingent consideration of $1,244,000 at acquisition date was determined by calculating a probability adjusted PBT for 31 December 2018 of between $1,100,000 and $1,300,000 and discounted to present value at acquisition date.

Note 6. Borrowings

At 30 June 2017 the following bank facilities were available to the Group:

- A three year facility of $147 million;
- A three year working capital facility of $3 million;
- A three year letter of credit facility of $3 million; and
- Ancillary facilities: credit card and electronic payaway facility of $12.5 million.

The banking facilities are guaranteed and secured by the Company and certain of the Company’s subsidiaries. The facilities are subject to a variable interest rate, which is based on BBSY plus a margin. The banking facilities mature on 29 July 2019.

The Group is subject to certain financing covenants and meeting these is given priority in all capital risk management decisions. These covenants include leverage and interest cover ratios, with reference to recurring earnings before interest, tax, depreciation and amortisation, and with distribution restrictions on dividends. There have been no events of default on the financing arrangements during the year.

Note 7. Equity - issued capital

Consolidated	**Date**	**Shares**	**Issue price**	**$'000**
Ordinary shares	31 December 2016	118,446,559		170,940
Ordinary shares - LFSP	31 December 2016	3,040,492		7,302
Ordinary shares - LFSP Management	17 March 2017	1,208,501	$6.39	7,722
Ordinary shares	2 May 2017	46,225	$6.49	300
Ordinary shares - LFSP CEO	3 May 2017	338,628	$6.50	2,201
Number of shares legally on issue	30 June 2017	123,080,405		188,465
Less: Unvested ordinary shares - LFSP	30 June 2017	(3,469,133)		(15,410)
Balance at 30 June 2017		119,611,272		173,055

On 15 February 2017, the board approved the vesting of 1,118,488 ordinary shares granted under the Loan Funded Share Plan (LFSP) in 2015.

On 17 March 2017, shares were granted to the management team under the LFSP at the market price, and at the Annual General Meeting on 3 May 2017, the CEO's 2017 LFSP grant was approved, with shares being granted at the market price. The shares granted as part of the LFSP are held by the participant until they vest or are forfeited and are eligible for dividends. Should the Company pay dividends or make capital distributions in the future, any dividends paid or distributions made to the participant will be applied to repay the loan and to meet the tax liability on those dividends or distributions. The shares are vesting on 31 December 2019. The vesting of the shares is subject to two performance hurdles, being an earnings growth hurdle (based on NPATA per share) and a total shareholder return hurdle.

At 30 June 2017, the unvested shares issued under the LFSP have been treated as contingently issuable, as all the vesting conditions have not been satisfied at the balance date. Therefore, the shares issued under the LFSP are excluded from basic earnings per share and included in diluted earnings per share.

Note 8. Equity - reserves

	30 June 2017 $'000	**31 December 2016 $'000**
Share-based payments reserve	3,117	2,367
Cash flow hedge reserve	(99)	264
	3,018	2,631

Notes to the financial statements (cont'd)

Note 9. Earnings per share

	30 June 2017 $'000	Restated 30 June 2016 $'000
Consolidated profit after income tax expense for the half-year attributable to the owners of Smartgroup Corporation Ltd	16,784	13,436

	Number	Number
Weighted average ordinary shares used in calculating basic earnings per share	119,611,272	104,270,139
Weighted average ordinary shares used in calculating diluted earnings per share	120,279,707	105,680,332

	Cents	Cents
Basic earnings per share	14.03	12.89
Diluted earnings per share	13.95	12.71

Note 10. Fair value of financial instruments

Fair value of the Group's financial assets and financial liabilities that are measured at fair value on a recurring basis

	30 June 2017 $'000	31 December 2016 $'000
Level 2 - Other financial assets - interest rate swap contracts	-	307
Level 2 - Other financial liabilities - interest rate swap contracts	(142)	-
Level 2 - Deferred consideration	(15,811)	-
Level 3 - Contingent consideration	(1,244)	(10,785)

The carrying amounts of trade and other receivables and trade and other payables are assumed to approximate their fair values, due to their short-term nature. The fair value of financial liabilities is estimated by discounting the remaining contractual maturities at the current market interest rate that is available for similar financial liabilities.

Derivatives - interest rate swap contracts
Derivative financial instruments have been valued using quoted market rates. This valuation technique maximises the use of observable market data where it is available and relies as little as possible on entity specific estimates.

Deferred and Contingent consideration arising on business combinations
At 30 June 2017, the deferred consideration arising on acquisition of Selectus is based on the final settlement amount, which is determined using actual Adjusted EBITDA for the 12 month period to 30 June 2017 and Company's share price at 30 June 2017.

In the comparative period, contingent consideration for Selectus is valued based on the likely settlement amount, discounted to present value. The fair value is determined using management estimates of future performance and the resultant potential liability. Significant unobservable valuation inputs in relation to contingent consideration include estimated Adjusted EBITDA and the Company's share price.

Contingent consideration arising on acquisition of TMG is valued based on the likely settlement amount and is discounted to present value. The fair value is determined using management estimate of future profit before tax ('PBT').

Notes to the financial statements (cont'd)

Note 11. Cash held on behalf of customers and associated liabilities

Cash held on behalf of customers recognised in the statement of financial position:

	30 June 2017 $'000	31 December 2016 $'000
Current assets - Restricted cash and cash equivalents	39,853	39,493
Current liabilities - Customer salary packaging liability	(39,853)	(39,493)

The restricted cash accounts are held with Australia's major financial institutions. Depending on commercial arrangements, the Group may earn interest income from these accounts. For the half year ended 30 June 2017, the Group has recognised finance revenue of $408,000 (30 June 2016: $18,000) from restricted cash.

Cash held on behalf of customers not recognised in the statement of financial position:

	30 June 2017 $'000	31 December 2016 $'000
Accounts established by the Group as cash held on behalf of customers	83,165	84,678
Accounts established by customers directly	66,067	71,368
	149,232	156,046

Cash held on behalf of salary packaging and share plan administration customers is deposited by customers into segregated bank accounts, to be used only to settle their employees' salary packaging obligations to suppliers or for contributions into share plans. The Group cannot use these funds for any other purpose than as directed by its customers. Customers are liable to ensure adequate funds are kept in the segregated bank accounts for salary packaging and share plan payments. The Group has assessed that these assets are held in a fiduciary capacity rather than being assets of the Group and as such, have excluded them from the statement of financial position.

The segregated bank accounts used for cash held on behalf of customers are with Australia's major financial institutions. Depending on commercial arrangements, the Group may earn interest income from these accounts. For the half year ended 30 June 2017, the Group has recognised interest revenue of $703,000 (30 June 2016: $590,000) from those accounts established by the Group as cash held on behalf of customers, as well as those accounts established by the customers directly. These amounts are recognised within outsourced administration revenue.

Note 12. Events after the reporting period

Selectus deferred consideration
In July 2017, the Group entered into agreements with two of the previous shareholders of Selectus whereby deferred share consideration, payable under the terms of the sale agreement, would be settled by the Group in cash in lieu of shares, at the equivalent of $6.56 per share. The relevant shareholders held 79.07% of the shares in Selectus at the time of the sale.

Based on the Selectus performance for the twelve months to 30 June 2017, the total deferred share entitlement of the Selectus vendors is 2,131,442 shares. Of this, 79.07% (1,685,331 shares) will be settled in cash at $6.56 ($11.1m) and the remaining 20.93% (446,111 shares) will be issued by September 2017. In addition, cash in lieu of dividends foregone of $0.8m will be paid to vendors by September 2017.

Directors declaration

In the directors' opinion:

(a) the attached financial statements and notes set out on pages 8 to 19 are in accordance with the Corporations Act 2001, including:

i) complying with Accounting Standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements, and
ii) giving a true and fair view of the consolidated entity's financial position as at 30 June 2017 and of its performance for the half-year ended on that date, and

(b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

Signed in accordance with a resolution of directors.

On behalf of the directors,

Michael Carapiet
Chairman
22 August 2017
Sydney

Independent auditor's review report to the shareholders of Smartgroup Corporation Ltd

Report on the Half-Year Financial Report

We have reviewed the accompanying half-year financial report of Smartgroup Corporation Ltd (the Company), which comprises the statement of financial position as at 30 June 2017, the statement of changes in equity, statement of cash flows and statement of profit or loss and other comprehensive income for the half-year ended on that date, selected explanatory notes and the directors' declaration for Smartgroup Corporation Ltd (the consolidated entity). The consolidated entity comprises the Company and the entities it controlled during that half-year.

Directors' responsibility for the half-year financial report

The directors of the Company are responsible for the preparation of the half-year financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the half-year financial report that is free from material misstatement whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express a conclusion on the half-year financial report based on our review. We conducted our review in accordance with Australian Auditing Standard on Review Engagements ASRE 2410 *Review of a Financial Report Performed by the Independent Auditor of the Entity*, in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the half-year financial report is not in accordance with the *Corporations Act 2001* including giving a true and fair view of the consolidated entity's financial position as at 30 June 2017 and its performance for the half-year ended on that date; and complying with Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*. As the auditor of Smartgroup Corporation Ltd, ASRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of a half-year financial report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Independence

In conducting our review, we have complied with the independence requirements of the *Corporations Act 2001*.

PricewaterhouseCoopers, ABN 52 780 433 757
One International Towers Sydney, Watermans Quay, Barangaroo NSW 2000,
GPO BOX 2650 Sydney NSW 2001
T: +61 2 8266 0000, F: +61 2 8266 9999, www.pwc.com.au

Conclusion

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the half-year financial report of Smartgroup Corporation Ltd is not in accordance with the *Corporations Act 2001* including:

1. giving a true and fair view of the consolidated entity's financial position as at 30 June 2017 and of its performance for the half-year ended on that date;

2. complying with Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*.

PricewaterhouseCoopers

Sam Hinchliffe
Partner

Sydney
22 August 2017

Corporate directory

Directors	Michael Carapiet Deven Billimoria John Prendiville Gavin Bell Andrew Bolam Ian Watt Deborah Homewood	**Auditor**	PricewaterhouseCoopers One International Towers Watermans Quay Barangaroo Sydney, NSW, Australia, 2000
Company secretaries	Amanda Morgan Sophie MacIntosh	**Solicitors**	Minter Ellison Lawyers Level 23, 525 Collins Street Melbourne, VIC, Australia , 3000 Tel: 02 9921 8888
Registered office	Smartgroup Corporation Ltd Level 8, 133 Castlereagh Street Sydney, NSW, Australia, 2000 Tel: 1300 476 278	**Bankers**	Australia and New Zealand Banking Group Limited 242 Pitt Street Sydney, NSW, Australia, 2000
Principal place of business	Smartgroup Corporation Ltd Level 8, 133 Castlereagh Street Sydney, NSW, Australia, 2000	**Stock exchange listing**	Smartgroup Corporation Ltd shares are listed on the Australian Securities Exchange (ASX Code: SIQ)
Share registry	LINK Market Services Level 12, 680 George Street Sydney, NSW, Australia, 2000 Tel: 1300 554 474	**Website**	www.smartgroup.com.au