PERSONAL FINANCIAL STRATEGIES

YOUR PERSONAL GUIDE TO WEALTH CREATION

Super or property: Issues to consider

The recent changes to superannuation have clouded the water for many when it comes to considering superannuation or property as the most effective wealth creation vehicle.

Superannuation has long been a regulatory nightmare. Recent changes simplifying the Superannuation rules came into effect on 1 July 2007, with some very generous bonus conditions including the opportunity to make a contribution of up to $1million before 30 June 2007.

If you missed that chance and are under 65 you can still take advantage of concessions and contribute up to $450 000 undeducted contributions over 3 years.

A super strategy?

What are the key issues when considering superannuation as a wealth creation strategy and how do recent changes affect property investors?

Tax-free redemptions

The new rules make superannuation redemptions after 1 July 2007 tax free for those over 60 years old. Additionally, these redemptions do not have to be treated as assessable income, ensuring income from other sources are taxed at a lower marginal rate.

Low or no tax on fund earnings

Investment earnings are taxed at a maximum rate of 15 percent. On the other hand, earnings outside super may be subject to tax as high as 46.5 percent. This is significant when you consider the after tax position of either option.

Furthermore, where superannuation benefits are rolled over to an allocated pension, earnings will be tax free.

Salary sacrifice

Employees under 35 have the greatest opportunity to make significant tax savings by salary sacrificing more into super because they will no longer be subject to the $15 260 annual limit on tax-deductible super contributions. Instead, their limit will be $50 000. Employees over 50 will have the same limit imposed, except for a limit of $100 000 per year transitional concession for a period of

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HELPING YOU MANAGE YOUR FINANCIAL FUTURE

We can help you keep your personal finances and wealth creation strategies on track.
Call us now and we'll arrange a meeting to discuss:

- Tax effective saving strategies
- Planning for retirement
- Minimising capital gains tax
- Property ownership
- Asset protection
- Selling your business

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five years. These limits set the total amount an employer will be able to direct into super on an employee's behalf, including both the compulsory super contributions and any salary sacrificed amount.

Salary sacrifice contributions will be taxed at 15% when it's received by the superannuation fund. From 1 July 2007, employer contributions, including salary sacrifice, of more than $50 000, or $100 000 for those over 50 years old, will be taxed at 46.5 percent.

The disadvantage of salary sacrificing is the fact money contributed to super can't be withdrawn until you reach your preservation age and retire. This is not a great concern for someone in their 50s because this group has a major motivation to salary sacrifice as much as possible.

No contributions tax

Property investors that sell a property and place the after capital gains tax proceeds into a superannuation fund (called the "non-concessional contribution" or after tax contribution), can contribute $450 000 over three years.

Property

Flexibility

Once your money is locked into your superannuation fund it cannot be accessed until you reach age 55 if born before June 1960, and age 60 for those born after June 1964. Another downside of superannuation is that you cannot use the money as security to borrow funds for any other purpose. Funds are basically quarantined.

Property on the other hand is more flexible in the sense that it can be sold to meet personal financial obligations. In many respects it is a lower risk vehicle for individuals who circumstances may change suddenly, such as having a family.

Property as leverage

Property investing is a method of wealth generation, distinct from superannuation. In principle, most wealth generation initiatives involve financial leverage or gearing (using borrowed funds) to acquire additional capital growth assets from the equity generated in your existing portfolio. Property, more often than not, serves as the basis of security to borrow additional funds to acquire assets. Provided that obligations on investment loans are maintained.

Capital gains tax benefits

Many individuals are using a self managed super fund to purchase property, on the basis that this will provide a means to minimise capital gains tax if the property is sold. Whilst there is an argument for this approach, there is a downside. Property held in a superannuation fund cannot be used as security for to leverage an expanding property portfolio. As a result, there are opportunity costs associated with not expanding a property portfolio in order to take advantage of future CGT benefits. The forfeited commercial gain may more than offset any tax saved.

Tax deductible expenditure

Wealth generation takes advantage of leverage to accelerate the net worth of individuals by the effective selection of capital assets and taking advantage of taxation benefits that accompany the borrowings for the asset acquisition. Property investing has some generous taxation concessions that allow taxpayers to claim cash and non-cash losses on annual property expenses as tax deductions off their primary income sources.

Deciding on a strategy of superannuation or property to build wealth requires some consideration, taking into account age, personal circumstances and income. Please feel free to contact our office to discuss any of these issues and how they make impact your wealth creation strategy.

MONEY TALK

Margin loans

Margin loans are a tool for gearing into share or managed fund investments. They essentially operate as a loan or line of credit that uses shares or managed funds as security for the facility. A margin loan is generally limited to a pre-determined value ratio of the portfolio. The available funds from a margin loan may rise or fall in line with the value of the portfolio itself. The lender is protected from falls in the security value when the value falls below the pre-determined ratio by utilising a technique referred to as a margin call. A margin call is a request for additional fund or assets (cash, shares, or managed funds) to bring the loan in line with the lending ratio.

What are managed funds?

Managed funds are investment vehicles that allow the pooling of financial resources with a number of other investors into a single fund. The fund is then able to invest in assets that might otherwise be out of the reach of any one investor. All managed funds have a document known as a prospectus which outlines where the fund manager plans to invest the fund members money.

Advantages

- Investment decisions are made by a fund manager
- Low entry costs
- Allows periodic additional capital cotributions
- Choice of investment fund eg property, equity
- Units have a market value and may be traded
- May be used as security to gear portfolio

Disadvantages

- Investments choices limited to choice of fund
- Investment decisions made by fund manager
- Investment returns are not guaranteed
- Administration costs
- Potential entry and exit costs

Emphasis on trustee understanding

The Deputy Commissioner of Taxation recently outlined changes for trustees designed to give a better assurance that they are aware of their obligations and responsibilities. These changes include a trustee declaration.

The trustee declaration has been introduced as part of the Government's plan to simplify and streamline superannuation and improve the regulation of self managed superannuation funds (SMSFs). The purpose of the declaration is to ensure that trustees (and directors of corporate trustees) acknowledge their understanding of obligations and responsibilities under the superannuation laws.

What is the trustee declaration?

From 1 July 2007, all new trustees (as well as directors of corporate trustees) of an SMSF are required to sign a declaration within 21 days of becoming a trustee or a director of the corporate trustee. The declaration aims to ensure that new trustees (or directors of corporate trustees) understand their obligations and responsibilities.

The declaration contains key information for managing an SMSF including information about:

- General trustee duties
- Investment restrictions
- The sole purpose test, and
- Record-keeping, reporting and lodgment obligations.

Esssentially, the declaration contains information trustees are obliged to know in order to manage an SMSF in accordance with the superannuation laws. By signing the declaration, trustees are acknowledging that they understand your obligations and responsibilities as a trustee (or a director of a corporate trustee).

Declarations must be signed if you became, on or after 1 July 2007, a new trustee (or director of a corporate trustee) a new or existing SMSF.

Planning your exit

Looking ahead to your departure from the business, you should have a plan to achieve your capital, and possibly your income expectations.

If you are going to retire and intend to have an ongoing income from the business, you need to take great care with your exit planning. To transfer the business with the minimum tax cost into one or more safe pairs of hands, you need to have a plan for transferring shares to selected younger family members, or for bringing them into ownership.

If you intend to sell the business, then you need to groom it for sale in order to achieve the best price. You should also be looking around for potential buyers - perhaps even your own staff, or competitors.

If the business will cease to operate when you retire, you still need to plan to collect the last debts, make the last taxation return and settle the final bills from your suppliers.

TEN POINTS TO CONSIDER

You can use many different strategies to maximise your wealth and minimise your taxes. The ones that will work best for you will depend on your unique situation. Start the review process by considering these ten questions. After you have completed this, simply call to discuss your needs. We would be pleased to help you develop a plan that achieves your financial goals.

	Yes	No
Is your business (including strategy) plan up-to-date and communicated firm wide?		
Do your plans include ways to grow the top and bottom lines?		
Are sales flat, growing only at the rate of inflation, or exceeding it?		
Is yours a service business with limited fixed assets, or are stock and equipment a large part of your company's value?		
What is the outlook for your line of business as a whole?		
Will your company's products and processes be outmoded in the near future?		
How competitive is the market for your company's goods or services?		
How strong is the company's staff that would remain after your sale?		
Do you have a sale or exit strategy that minimisation taxation and ensures you realise the maximum value for your business?		

My greatest planning concern/need is

Term allocated pensions deadline

Changes introduced as a part of the 2006 Federal Budget will soon eliminate the benefits of term allocated pensions (TAP). The new Government rule also creates a significant Centrelink disadvantage for those retirees who do not act soon.

What is a TAP?

A term allocated pension is simply one product that you can buy with proceeds from a superannuation fund when you retire. A TAP is an investment which pays a regular and tax effective income stream in retirement for a set term, and can be purchased from a number of financial institutions.

How does a TAP work?

Money from a superannuation fund is invested in a TAP. The TAP in turn invests the funds in an allocation of assets chosen by the investor, and pays a regular income comprised of interest and capital until your account runs out at the end of the fixed term, often based on life expectancy.

Income payments from a TAP are not guaranteed. They may rise or fall in line with the value of investments selected as part of the asset allocation. Whilst the term is set, the level of payments are not and are calculated at the beginning of each financial year according to a set formula, based on the current account balance and the remaining term. The formula is designed so that the account balance is reduced down to nil by the end of the term.

Generally, once money is invested in a TAP, it cannot be taken our in lump sums or converted to some other form of products that allows lump sum payments. The decision to purchase a TAP is one that needs to be made carefully.

Changes ahead

TAPs are complying income streams for Centrelink purposes and can be purchased at any age. Currently, 50% of the purchase price of a TAP is exempt from the assets test. This will change from 20 September 2007.

Term Allocated Pensions (TAPs) purchased after 19 September 2007 will be fully assessed under Centrelink's assets test. However, TAPs purchased between now and 19 September 2007 will retain their 50% assets test exemption throughout their term.

In other words, if a TAP is purchased before 20 September 2007, half the money invested in it will not be counted for the Age Pension assets test for the full term of the TAP (which can typically be 18 or more years). So for example, an investment of $150 000 will result in only $75 000 being assessed as an asset by Centrelink. That means individuals near the upper threshold limit of assets who commence a term allocated pension after 20 September could find themselves missing out on a pension altogether

This presents a significant planning opportunity for those recieving an aged pension or for those seeking to become eligible. There is limited time to take advantage of the changes. If you are uncertain about how these changes may affect you please contact our office.

A Great Read

The Roaring 2000s

Author Harry Dent Jnr

Almost a classic, The Roaring 2000s, focuses the full spectrum of changes that will follow in the wake of the turn-of-the-century economy.

According to Dent, how and where we work and live is about to change more drastically than at any time in our history due to the convergence of the mainstreaming of the Internet and other technologies and the peak spending years of the aging baby boomers. This will result in nothing less than the greatest boom in history and an unprecedented opportunity for investors and entrepreneurs who anticipate these changes.

Dent not only offers detailed wealth creation strategies aimed at exploiting the coming boom for the next two decades but he also explains future trends in the job market, technology, demographics, and real estate. He predicts the next great population migration and explores the radically different business and organisational structures that will be the offspring of the Information Age.

Despite having been written over a decade ago, the Roaring 2000's provides a powerful lesson about how a clear understanding of demographics and economics provides insight into trends in consumption, spending and saving. Armed with this understanding investors are able to identify opportunity in a range of new and developing markets.

We are sometimes asked if we are able to help additional clients. We are a growing firm and do appreciate your referals. We consider it a compliment when you recommend us to your friends and business contacts.