

# your money your future

FINANCIAL PLANNING NEWSLETTER SUMMER 2006

## Merry Christmas & Happy New Year

Welcome to the final edition of the HPH Hotline for 2006.

It's been a remarkable year in terms of growth for both clients and HPH. We're currently reviewing our client value proposition in conjunction with external consultants, to ensure we continue to improve and deliver the highest quality advice and service to you in 2007.

HPH received industry recognition with Rob making the top 50 of AFR Smart Investor's Masterclass 2007 and Adam a finalist in the 2006 AFA Adviser of the year award.

2007 is shaping to be an exciting year, in particular the proposed budget changes from 1 July onwards.

Please enjoy the Xmas break and we hope you and your family have a happy, healthy and prosperous new year!

Cheers Rob, Adam and the Team at HPH.

## The Budget's big superannuation sweetener

**In May each year, the Federal Treasurer delivers the Government's Budget. The Budget speech reports on the Government's previous expenditure and the spending initiatives for the coming years.**

This year the Treasurer unveiled the biggest shake-up to the superannuation system for more than 20 years. From July 2007, contributing to superannuation and withdrawing it in retirement will become simpler, more flexible and more tax-effective.

In September the Treasurer sweetened the original Budget statement by introducing some new opportunities

to contribute to your superannuation savings. The big sweetener is that until 30 June 2007, eligible Australians can contribute up to \$1 million in undeducted contributions. After 1 July 2007 the amount will be capped at \$150,000 pa (or \$450,000 over three years for people under 65).

This one-off opportunity will give many Australians a chance to significantly boost their superannuation savings.

To find out how to improve your retirement prospects, speak to your financial adviser.



### HPH Hotline HPH Solutions

Rob Pyne & Adam Smith

HPH Solutions  
Level 1, 35 Outram Street  
West Perth  
WA 6005

**Rob Pyne** BSc. F.Fin CFP Retirement Planner

**Adam Smith** Dip FP CFP Risk Specialist

### Authorised Representatives

Po Box 1798  
West Perth  
WA 6872

Phone: 08 9213 0444

Fax: 08 9226 4933

Email: [rpyne@hphsolutions.com.au](mailto:rpyne@hphsolutions.com.au)

Email: [asmith@hphsolutions.com.au](mailto:asmith@hphsolutions.com.au)

Web: [www.hphsolutions.com.au](http://www.hphsolutions.com.au)



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## The benefits of multi-manager investing

### What is a multi-manager fund?

A multi-manager fund provides investors with the opportunity to invest in a single fund and benefit from the investment management styles, strategies and different approaches of a range of fund managers.

A multi-manager fund pools together the funds of individual investors – as does a fund managed by a single investment manager. However, a multi-manager fund allocates a portion of the invested funds to several fund managers who may each specialise in a particular:

- investment technique;
- investment sector;
- asset class;
- industry;
- economy;
- management strategy; and/or
- investment style.

The aim of a multi-manager fund is to bring different managers, investment strategies and techniques together with the aim of providing opportunities for increased diversification and, thereby, delivering more consistent and competitive returns over the long term.

Some of the benefits of multi-manager investing include:

#### • Consistent, above-market performance

Multi-manager funds are designed to deliver consistent returns over most stages of the economic cycle. These returns are achieved by combining fund managers with different, complementary approaches to investing.

By diversifying your investment with a range of investment managers, you can decrease the variability in your investment returns. By spreading your investment between fund managers, you are reducing the effect of any one manager on your overall investment return. This means you are more likely to achieve your investment objectives, providing the multi-manager fund you have chosen meets your investment objectives.

#### • Cost-effective and convenient

Through a portfolio that is regularly balanced, multi-manager funds provide you with access to a variety of fund managers and asset classes without the paperwork and cost of doing it yourself.

#### • Diversification – an excellent way of spreading your risk

When you invest in a multi-manager fund, your investment dollar is spread across a number of specialist fund managers and approaches to investing, such as 'value' and 'growth'. This may help to improve returns and reduce risk. It also reduces the reliance placed on any single fund manager.

#### • Access to niche investment opportunities

Multi-manager funds can give you access to some investment opportunities and fund managers that may not normally be available to you as a retail investor including boutique fund managers and specialist managers located overseas.

#### • Quality research to uncover the world's best fund managers

With more than 50 Australian share managers and hundreds of Australian and international fund managers offering international share funds, it can be difficult to know where to invest.

Multi-manager investors benefit from careful manager selection based on thorough research and analysis designed to identify the best fund managers for each role in the fund.

#### • Ongoing monitoring

Ongoing regular research goes into the selection and retention of fund managers in quality multi-manager funds to detect any changes that may impact future performance. In a quality multi-manager fund, those managing your money are monitored each day to ensure they are on track. Regular monitoring and research, combined with fast, efficient changes where required, can give you confidence that your investment is being actively managed.

#### • A strategy that keeps up with changing market conditions

In an investment climate that is constantly changing, it's difficult keeping up-to-date and ensuring your investment strategy and fund managers remain appropriate. Investors in a quality multi-manager fund need to be confident that any changes to investment markets and fund managers will be identified and assessed and their investment portfolio amended accordingly.

#### What are the next steps to getting started?

Contact your financial adviser today to see if a multi-manager strategy is right for your financial situation. Your financial adviser can help explain the benefits of multi-manager investing further and work with you to see how to incorporate multi-manager investing into your financial plan.



## Super up, tax down – an opportunity to boost your retirement savings before 1 July 2007

When it comes to your investments, whether or not assets are held in superannuation or in your personal name can make a big difference to the amount of money you receive in retirement. This is because of the different ways in which the Federal Government taxes superannuation benefits and personal investments.

### A short-term window to convert your assets to super

As a result of the Government's recent Budget announcements, there is a short-term window of opportunity in which you can maximise your tax-free contributions into superannuation. Before 1 July 2007 it is possible to make undeducted contributions up to \$1 million. After this date, a cap of \$150,000 per year will generally apply.

An undeducted contribution is made with money you already have paid tax on. As such, no further tax is paid by your superannuation fund when it is contributed.

### Sell now or sell later?

For many people, the \$1 million limit up to

1 July 2007 means it may be worthwhile selling assets held in personal names, such as shares and property. Then, after accounting for any potential capital gains tax (CGT) liability, the remaining funds can be invested in superannuation. Further, any capital gains liabilities may be reduced or eliminated using other simple advice strategies.

The diagram below highlights two scenarios:

1. Sell later – this shows the result of leaving investments in your own name until they are needed in retirement. Here, CGT will be paid at your personal tax rate when the asset is sold, eroding the total gain from the investment.
2. Sell now – this shows the result of converting a personal asset into superannuation. Firstly, the asset is sold, and any CGT liability is paid. The remaining funds are then contributed into superannuation, where the tax rate on income and capital gains is usually lower than your personal tax rate.

### Case study – selling shares for a long-term super advantage

Helen, aged 54, works as a dentist in Brisbane and has recently been contemplating how to maximise her retirement wealth. In 2001, she received an inheritance from her aunt and subsequently had purchased a share portfolio worth around \$190,000. In June 2007, the portfolio is worth around \$263,000.

Assuming that all dividends are re-invested, the shares would be valued at around \$540,000 in 10 years' time. If the shares were sold in 10 years, Helen would incur a CGT liability of approximately \$37,000, leaving a net value of \$503,000.<sup>1</sup>

As an alternative, Helen considers selling the shares before 1 July 2007 and contributing the proceeds into superannuation. In the future, when the fund is in pension phase, the assets can be sold without any CGT liability.

If Helen sells the shares in June 2007, she will have a capital gain of \$35,200. Because of the 50 per cent reduction for assets held for more than one year, a gain of \$17,600 would be included in her assessable income. This will incur a CGT liability of around \$7,300.

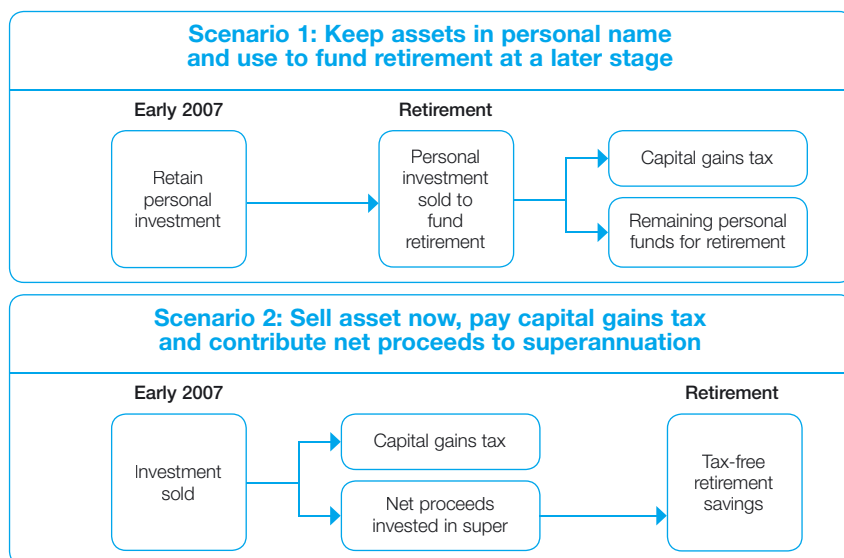
Helen contributes the sale proceeds into superannuation. In 10 years, assuming the same rate of growth and dividend yield, this portion of her superannuation fund will be worth around \$600,000. For Helen, this means the benefit of converting her assets amounts to approximately \$97,000 (ie \$600,000 less \$503,000).

### Other considerations for converting

Before converting your assets to superannuation it is important to fully understand the tax implications and the preservation rules of superannuation. In addition, it may be worth investigating the possibility of starting a non-commutable allocated pension, which may further enhance the strategy.

For more information on boosting your retirement savings, speak to your financial adviser.

<sup>1</sup> Assumptions: 4% capital growth; 4% dividend yield – fully franked; after-tax dividend reinvested; CGT payable on disposal paid by selling shares; marginal rate of 41.5%.



### Why convert personal investments into superannuation?

The simple answer is because of the tax benefits. Despite having to pay capital gains tax on any immediate investment profit, the tax benefits of an investment in superannuation can, over time, out-pace the comparative gains of leaving the asset in your personal name. Other advantages may include:

- Boosting your superannuation in preparation for a tax-free income stream in retirement (Note: superannuation income for people over age 60 is tax-free from 1 July 2007.)
- Income from the superannuation assets will be taxed at a maximum rate of 15 per cent compared to your marginal tax rate if assets are held personally. Better still, in pension phase there is no tax on earnings.
- You may be eligible to claim a tax deduction for all or part of the contribution.

## Business succession planning

**Without a business succession plan, the death or disablement of a business partner could be catastrophic. However, many small businesses fail to address succession planning believing that such a catastrophe will not happen; considering the process too long or too expensive; or putting succession planning off until things 'quieten down'.**

### Case study

The following case study illustrates how things can go wrong without a business succession plan.

Gary, aged 45, and Richard, aged 52, are directors and equal shareholders in a consulting engineering firm with an estimated net market value of \$3.6m.

Tragically, Richard dies leaving behind his wife, Alice, and two young children. Other than the family home, his interest in the business was his main asset, which passes to Alice under his will.

Prior to death, the business had relied heavily on his involvement. As a result of his departure, significantly less revenue will be generated. Gary knows he should employ someone to replace Richard but is concerned about cash flow.

Richard and Gary provided personal guarantees of \$600,000 to cover the debts of the business. Under the terms of the loan agreement, the outstanding debt is immediately repayable following Richard's death. Gary has managed to refinance the debt, albeit, at a higher interest rate. This is fortunate for Alice as Richard's estate would have been jointly and severally liable due to the personal guarantee he provided.

Alice needs cash urgently as she is having difficulty meeting living expenses without Richard's salary. Alice and Gary previously had a good relationship but this has deteriorated following ongoing disagreements over the amount she will receive for Richard's share of the business.

In addition to the pressure of managing the company without Richard, Gary realises he is now in business with Alice, as she now controls 50 per cent of the company – a situation likely to result in further conflict.

The above scenario could have been avoided by appropriate planning. Let us assume that Richard and Gary had consulted a financial adviser who had recommended the following:

- key-person insurance; and
- an insurance funded buy/sell agreement.

### Key person insurance

The cost of replacing Gary or Richard in the business, together with the expected loss of profits as a result of the disruption to the business, was estimated at \$500,000. Gary and Richard also intended to protect their families from any liability due to the personal guarantees each of them had provided for the business debts (currently \$600,000).

Accordingly, Gary and Richard were advised to take out key-person insurance for \$1.1m over each of their lives. This would provide a lump-sum benefit to the business in the event of the death or disablement of either Richard or Gary as key persons.

In the above case study, key-person insurance would have allowed Gary to employ someone appropriately qualified to replace Richard. It would also have cleared the business debts and replaced the short-term loss in revenue as a result of Richard's departure from the business.

### Buy/sell agreement

A buy/sell agreement is an arrangement for the transfer of a deceased or disabled owner's interest in the business to the remaining owners. This ensures that the departing owner (or their family or estate) receives fair market value for their interest in the business. It also ensures the remaining owners have exclusive ownership and control of the business.

Insurance is commonly used to fund the purchase of the business interest under a buy/sell agreement. This is because

an insurance funded buy/sell agreement avoids the need for the remaining owners to finance the purchase of the business using additional debt or using other resources.

Following advice from their financial planner, Gary and Richard entered into a buy/sell agreement funded by insurance policies covering death, disablement and trauma.

In the above case study, pursuant to the buy/sell agreement, Richard's 50 per cent shareholding in the business would be transferred to Gary following his death. Alice would receive \$1.8m which was the amount of the insurance policy taken out to fund Richard's side of the buy/sell agreement. In essence, the buy/sell agreement would have ensured Alice and Gary received what they needed at the time of Richard's death.

### Implementing a business succession plan

The first step involves talking to your financial adviser who will often need to work closely with your solicitor and accountant. While your solicitor will be involved in drafting the buy/sell agreement and updating your wills, your accountant will typically be involved in determining the financial impact of the loss of a key person and the price to be paid under the buy/sell agreement. In addition to helping you through the entire process, your financial adviser can help you identify the most appropriate key-person insurance and help to arrange the buy/sell agreement.

