WEALTHMATTERS

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INSIDE

- Reverse mortgages: a retirement solution
- Boost your retirement savings
- Preparing for the super changes
- Preparing to help out parents financially
- Common errors when investing
- Investing in property through an SMSF

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Protecting your finances after separation

The end of a relationship is a particularly difficult time for most individuals - among the emotional pain comes burdensome administrative tasks, such as sorting out finances.

Although these tasks may seem tortuous; it is best to address financial issues promptly to safeguard your finances against misuse and ensure peace of mind.

Here are three things to consider when protecting your finances after separation:

Joint accounts

If you think your former partner may exploit your finances, it is worth considering closing your joint accounts. Both account holders need to agree that the accounts should be closed. You will need to discuss how the remaining balance will be divided with your former partner, as you must have zero funds in the account before closing it. It is then necessary to establish your own account and redirect any direct debits or credits from your joint account to your new account (or make alternative arrangements).

Your Will and power of attorney

Your Will may not be the first thing to come to mind after a breakup, however, it is a critical document that needs to be reviewed, especially if your former partner is listed as a beneficiary or executor. After separating, review your Will with a legal professional to make any necessary changes. If you appointed your former partner as your power of attorney, you might also consider revoking them upon separation. Again, a legal professional can aid you with this decision.

Home and other joint loans

Upon separation, it is best to advise any lender/s of your separation and the arrangements for paying the loan. Notify your bank if you wish to discontinue any redraw facilities or linked credit cards attached to your loan. Ask your bank for a written confirmation letter and keep a copy in case there are any issues down the track.

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Reverse mortgages: a retirement solution

Changes to the age pension assets test have left many retirees looking for alternative sources of income to fund their retirement.

On 1 January 2017, the assets test limit for part age pension rates dropped to $542,500 (from $793,750) for singles, and $816,000 (from approximately $1.1 million) for couples; and the taper rate doubled to $3 per $1000 a fortnight.

While some retirees have benefited from these changes, many have or will suffer, prompting a vast majority of retirees to consider other sources of income to continue living comfortably in retirement.

An appealing option for asset-rich, cash-poor retirees i.e. older homeowners with little income - is to take out a reverse mortgage.

A reverse mortgage allows retirees to access money without having to sell their house. It is a type of home loan that allows the homeowner to borrow money using equity in their home as security. The home loan can be taken as a lump sum, a regular income stream, a line of credit or a combination of these options.

Just like a normal loan, interest is charged on a reverse mortgage. However, borrowers don't have to make repayments while they continue to live in their home. Instead, the interest compounds over time and is then added to the loan balance.

If the borrower passes away, moves into aged care, or the time has simply come to sell the home, the loan (including interest and fees) must be paid in full.

Similar to most strategies concerning finances and wealth, there are risks associated with reverse mortgages that shouldn't be underestimated.

The decision to take out a reverse mortgage should be based on interest rates, fees and features, legal, establishment and ongoing costs and homeowner obligations.

Interest rates for reverse mortgages are generally higher than average home loans and can vary between providers. The amount that can be borrowed also varies. For example, those who are 60 years of age can generally borrow 15 to 20 per cent of the value of their home. This usually rises by 1 per cent for each year older than 60.

Boost your retirement savings

Pre-retirees can take advantage of a range of strategies to boost their nest egg.

Here are three popular ways to top up your retirement savings:

Maximise contributions

Take advantage of the concessional (pre-tax) and non-concessional (after-tax) contributions by contributing as much as you can afford before reaching the caps. From 1 July 2017, the annual concessional contributions cap will be $25,000 for all age groups.

Consider spouse contributions

Spouse contributions are super contributions made on behalf of your spouse. Generally, you can claim a tax offset of up to $540 per year if your spouse is a low-income earner or is not working. From 1 July 2017, the spouse's income threshold will be increased to $40,000 to assist more couples to support each other in saving for retirement.

Keep on working

The longer you work means more time to leave your savings untouched and additional time to contribute to super. Delaying retirement leads to a shorter retirement and hence more savings. You may also consider working part-time to enjoy income while waiting until Age pension age.

Preparing for the super changes

Tighter superannuation rules will apply from 1 July 2017 as part of the super reforms announced in last year's Federal Budget.

The new rules include the introduction of a $1.6 million super balance cap for after-tax contributions; a maximum of up to $25,000 for concessional contributions; and the removal of the current "bring-forward" rule allowing $540,000 of contributions in one year.

Although the new rules will come into effect from 1 July 2017, individuals can take advantage of the current rules to top up their nest egg.

Individuals under 65 who wish to make a large contribution, in particular, those with inheritances or who have recently sold a property or other large asset can make the most of this last-chance opportunity to contribute up to $540,000 until 30 June.

From 1 July 2017, individuals will only be able to bring forward up to three year's worth of after-tax contributions, i.e $300,000 over three years.

The bring forward rule cannot be accessed by those aged between 65 and 74 who meet the work test, however, they can still make annual after-tax contributions.

Those with balances in excess of the $1.6 million cap will need to review their super before 30 June to continue to make after-tax contributions. Furthermore, individuals with a balance close to $1.6 million will only be able to bring forward the annual cap amount for the number of years that would take your balance to $1.6 million.

Common errors when investing

Whether you are a first-time or experienced investor, the stakes are high when it comes to investing. Even the most savvy investors can fall into the trap of bad investment habits.

Although there is no guaranteed formula for investment success, there are some mistakes to watch out for:

Chasing performance

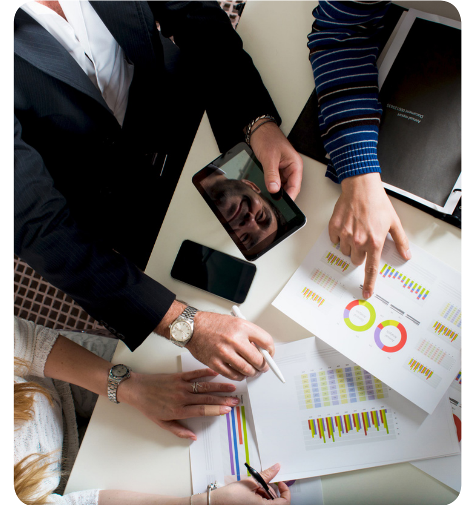
Basing investment decisions on strong, recent performance instead of judging them on their risk/reward merits is one of the biggest offenders. If an asset class, strategy or fund has been outperforming in the past few years, it may be nearing its end. Removing long-term strategic investments to chase these short-term, high performing investments may seem like a smart move but can be costly. Investors should instead focus on their long-term investment strategy and participate in a regular rebalancing of its asset allocation.

Poor diversification

Diversification helps create an investment portfolio with varying asset classes and securities to meet different levels of risk and return in various market scenarios. Under-diversification involves excessively-concentrated portfolios, such as holding just a few stocks - but this can have devastating effects if the market moves against a particular asset class. Ensure your investment portfolio is well-diversified for optimal performance and to protect against volatile market conditions.

Expecting too much

No one can predict or control market returns; successful investing takes a lot of patience and self-evaluation. Your investment goals should be reflected in your asset allocation to match your risk profile and life goals. For example, those with a higher tolerance for volatility can invest more of their portfolio in assets, such as shares and property, whereas conservative investors may be better suited to a higher allocation of income assets like fixed interest and cash.



Investing in property through an SMSF

It is vital for those with a self-managed super fund (SMSF) to carry out the necessary checks before purchasing a property in their SMSF, especially where borrowing is involved.

Investment strategy

The SMSF's investment strategy must be considered. If the purchase of a property will cause the fund's other investments to be out of alignment, trustees should consider amending the investment strategy before purchasing a property.

Resources

Trustees need to consider whether the fund will have the resources to purchase the property. For example, will the SMSF purchase the property using its available resources or would it be wiser to purchase a property of greater value using borrowed funds.

Structure

Once trustees have decided on the property to be purchased, the next step is to consider the structure in which the property will be owned. For example, SMSF trustees can own the property or organise for their SMSF to own units in a unit trust that will own the property.

Borrowing

After deciding on the structure in which the SMSF trustee will own the property, the next decision is often whether the fund will enter into an SMSF limited recourse borrowing arrangement (LRBA). Trustees should determine whether the borrowing will be from a bank, another financial institution or a related party. If a related party is loaning the money, trustees must ensure the loan is on commercial terms.

Members purchasing property through debt have several restrictions on their investment under the limited recourse borrowing arrangement (LRBA). To establish a LRBA, a 20-35 per cent deposit is required and enough money to cover stamp duty and legal expenses within the SMSF, or ready to roll over from another super fund.

The fund will be assessed on its borrowing potential based on member's superannuation contributions and the rental income from the property. Lenders will often require a personal guarantee from the SMSF trustees as the lender can repossess the property if an SMSF cannot meet its repayments.

Management

Once the SMSF has purchased an asset like property, trustees need to consider what would happen in the event of the death of a member. For example, the property may need to be sold or transferred to beneficiaries. Or, if a surviving spouse is to be the recipient of the death benefits, then the funds could remain in the SMSF to provide a pension to the surviving spouse.

Liquidity

As property is a large illiquid asset, the fund should have enough cash on hand to pay day-to-day expenses. If the property is the only asset in the SMSF and it is in pension phase, it may not be able to supply a sufficient retirement income to its members.

When determining what would happen in the event of the death of a member, trustees should also consider other events, such as the disability of a member. Planning for this should take place at the time of purchase, as SMSF's can incur significant financial difficulties if a member becomes disabled.

Preparing to help out parents financially

When providing financial assistance to parents, it is important to consider all possible outcomes and document intentions carefully.

For those planning to give their parents significant financial help, there are a number of options available. However, to decide on the right option, holding a family discussion to discuss the relevant aspects of a strategy and documenting the result can be very useful to refer to in the future.

Family discussions can also ascertain the view of each family member; it is possible that the children feel that the money will be best spent securing the retirement well-being of their parents. It is a good idea to discuss exactly where the money given to parents will be spent, and the amount and frequency of contributions.

Before providing financial support to parents, it is essential to review your personal financial situation. Discuss your options with your partner or spouse and come up with a plan of how much you can realistically allocate towards your parents' expenses.

Drawing up a budget helps to avoid overextending yourself and letting go of your own financial priorities. It is especially useful for those who plan on providing long-term financial assistance to parents.

Many issues can arise when children financially help out their parents, especially upon a parent's death. It is common for children who have helped out parents more than their siblings to feel a sense of entitlement when it comes to inheriting part of their parent's estate.

To avoid potential legal issues, children who give money to parents need to be clear whether the money is considered as a 'gift' or loan. For those who provide a loan to their parents, it is a good idea to get it writing and ensure the loan will be reflected in the parent's will.

For siblings who decide to help out their parents together, i.e. purchasing a property together for their parents to live in, caution must be taken. Siblings need to consider what will happen in circumstances where one or more siblings become unable to make mortgage repayments and so forth.

Before purchasing property together, siblings need to create an agreement in writing with each party obtaining proper and independent legal advice. While this may seem unnecessary in family situations, it is not uncommon for a person's circumstances to change resulting in them unable to pay the bills. Creating, understanding and setting rules can minimise or avoid conflict later on.

Overall, it is critical for all parties involved to be open and honest about their financial situation and intentions. Starting the conversation before money is lent or given is the best way to savour the health of your relationships and ensure all family members are on the same page. Obtaining professional advice before making financial decisions is recommended to avoid future disputes.

Why use a BDBN?

Using a binding death benefit nomination (BDBN) can provide members with the peace of mind knowing that their superannuation will be protected and properly distributed in the event of their death.

A binding death benefit nomination is a legally binding written document which outlines who you wish to receive your superannuation benefit if you were to pass away. For a BDBN to be legally binding, it must be 'valid.'

For a BDBN to be valid, the person or people you nominate to receive your superannuation benefits must be classified as dependents. Under Australia's superannuation laws, dependents include spouses; children of any age; individuals who are financially dependent on the deceased; a legal representative or individuals who are in an interdependency relationship with the deceased.

There are two types of BDBNs; lapsing and non-lapsing. A 'lapsing' BDBN remains in effect for three years from the date it is first signed, last amended or confirmed.
A 'non-lapsing' BDBN will not expire unless the trustee amends or revokes it. Members can amend or revoke their BDBN at any time.

To make a valid BDBN, the document must include certain information and elements, such as the proportion of the benefit to be paid to each beneficiary nominated; the signature of the member (the member must sign the form in the presence of two witnesses who are over the age of 18) and witness declarations.

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